In the Supreme Court of the United States

OCTOBER TERM, 1939

No. 181

HERBERT FLEISHHACKER,
Petitioner,

vs.

LUCIEN BLUM, EDMOND LANG, ELIZABETH LANG, RENE FOULD, ESTHER FOULD, MAX LAZARD, ROGER HAAS, ANDRE HAAS, LUCIE EMILE LEWYLIER, S. A. JOHANESSON, G. O. HOFFMAN and HENRY LEON,
Respondents.

Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Ninth Circuit and Supporting Brief

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Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Ninth Circuit

To the Honorable, the Supreme Court of the United States:

Herbert Fleishhacker prays that a Writ of Certiorari issue to review the decision (R 924) of the Circuit Court of Appeals for the Ninth Circuit made in the above entitled cause on February 7, 1940, which affirms the decision of the District Court for the

Northern District of California, Southern Division, as against Petitioner, rendered March 29, 1938. (R 320)

SUMMARY STATEMENT OF THE MATTER INVOLVED.

This is a stockholders' suit to recover an alleged secret bonus or bribe received by the President of a National Bank (Petitioner herein) for allegedly procuring a loan of the Bank's funds.[1]

The loan, amounting to $325,000, was made in December 1919. It was secured by Liberty Bonds, and was repaid in four months.

Fourteen years later, on December 5, 1934, twelve French citizens holding 1554 shares of stock of the Bank[2] out of 770,000 outstanding, some of whom

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(1) This then was and still is a criminal act. 12 U. S. C. Sec. 595 reads:

> "Except as herein provided, any officer, director, employee, or attorney of a member bank who stipulates for or receives or consents or agrees to receive any fee, commission, gift, or thing of value from any person, firm, or corporation, for procuring or endeavoring to procure for such person, firm, or corporation, or for any other person, firm, or corporation, any loan from or the purchase or discount of any paper, note, draft, check, or bill of exchange by such member bank shall be deemed guilty of a misdemeanor and shall be imprisoned not more than one year or fined not more than $5,000, or both."

(2) The bank is the Anglo-California National Bank of San Francisco. At the time of the loan its name was Anglo and London Paris National Bank of San Francisco.

were then engaged in other litigation against the Bank and its President, filed this suit.[2] Their purpose in initiating the matter was to obtain proofs of frauds that might aid in the other litigation. (R 459)

On March 29, 1938, the District Court entered judgment against Petitioner for $736,485.57 (being $348,125 alleged bribe, and $388,360.57 interest thereon).[3]

The Background.

L. B. Barde and J. N. Barde were brothers conducting a general steel business in Portland, Oregon, through a corporation, M. Barde & Sons, Inc. (R. 176)[4] which on December 23, 1919, had a net worth of $750,000. (R 180, 607)[4] For some time they had done business with the Bank and enjoyed an unsecured credit line of $111,000. (R 176)[4]

The Bardes knew Petitioner: one of them had married Petitioner's cousin. On numerous occasions they had sought to interest Petitioner in various ventures on a 50-50 partnership basis. Petitioner was a man of large means and engaged in many business enterprises. (R 621, 654-63, 701-4)

The Partnership Agreement.

Some time prior to December 1919 L. B. Barde invited Petitioner to become a 50-50 partner with the Bardes in a venture to buy and resell surplus

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(2) These are the Respondents herein. For convenience they are referred to as plaintiffs.

(3) Petitioner's affairs are now in the bankruptcy court.

(4) This fact found by trial court in its opinion.

wartime steel of the United States Shipping Board of the value of about $40,000,000. (R 176)[1] The capital required, in cash or credits, was $1,000,000. (R 176)[1] The proposal was that the Bardes would supply $500,000 in cash and Petitioner $500,000 in cash, securities, or a bond, as required by the Shipping Board (R 177)[1] and each was to receive a half interest in the enterprise. (R 176)[1] This was agreed to between L. B. Barde and Petitioner, subject to an investigation as to the feasibility of the venture. (R 177)[1] The actual requirements of the Shipping Board as to security were not then definitely known. (R 702)

Investigation convinced the parties that the venture was promising, (R. 664, 702) and L. B. Barde ascertained that the Shipping Board requirements would be earnest money of $250,000 with the bid; and if accepted, the contract must be secured by $400,000 in cash, and by a surety bond of $500,000. (R 176)[1] It was estimated that cash working capital of $100,000 would be required. (R 176)[1] This made the total requirements $500,000 cash (to be supplied by the Bardes) and $500,000 surety bond (to be supplied by Petitioner, who had agreed to supply cash, securities or a bond as required by the Shipping Board). (R 177, 702)[1] The parties agreed to proceed on these terms as originally proposed. (R 177, 298)[1][2]

At this time, as the trial court found in its opinion, it had not been suggested to Petitioner that the Bardes

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(1) This fact found by trial court in its opinion.

(2) This fact found by trial court in its formal findings.

would want to borrow from the Bank to finance their capital contribution, (R 177)[1] and Petitioner believed the Bardes had the cash to finance their share. (R 675, 696)

The Loans.

When the time came to put up the money, and not until then, (R 177, 298) [1] [2] the Bardes informed Petitioner they desired to borrow and asked whether they could borrow at the Bank. (R 177)[1] Petitioner presented their application to the Bank's Finance Committee (R 624-6, 634, 645-6, 678-9, 681, 700) its lending agency (R 204, 678), which was advised by Petitioner (R 629, 646-7) and knew that the proceeds were to be used by the Bardes in this venture and that Petitioner had a half interest therein as a partner. (R 176, 190)[1] Petitioner recommended the loans as safe loans, which fact the trial court found true. (R 178, 186)[1] The Finance Committee, Petitioner not acting, authorized loans aggregating $325,000 to the Bardes, on 6% demand notes of M. Barde & Sons, Inc. endorsed by J. N. Barde and secured by $225,000 to $250,000 of Liberty Bonds. (R 178-9)[1] As already noted, the Bardes had done business with the Bank for some time and enjoyed an unsecured credit line of $111,000. (R 176)[1]

The fact that Petitioner was a partner in the venture and that the proceeds were to be used therein,

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(1) This fact found by the trial court in its opinion.

(2) This fact found by the trial court in its formal findings.

were common knowledge in the Bank at the time. (R 190, 313, 428-9, 604-5, 611-12, 624, 629, 679, 700) The Bardes obtained the remaining $175,000 of cash for their capital contribution by borrowing at the Central National Bank of Oakland, on their note guaranteed by Petitioner. (R 179)[1]

Petitioner supplied his agreed 50% contribution by obtaining a $500,000 surety bond from the Fidelity and Deposit Company of Maryland, executing therefor his personal indemnity in that amount. (R 86, 181)[1] This bond was accepted by the Shipping Board and continuously secured the faithful performance of the contract of purchase. (R 86, 181, 303)[1][2]

The Shipping Board having accepted the bid, the Barde Steel Products Corporation[3] was organized to conduct the venture. Its stock was issued one-half to the Bardes and one-half to Petitioner's nominees.

The venture proceeded. Within four months the Steel Corporation repaid the $325,000 loan made by the Bank to the Bardes, charging the partners therefor on its books—Petitioner being charged one-half. Petitioner's liability on his $500,000 bond continued thereafter, and until termination of the contract with the Shipping Board.

The Profits.

Petitioner received from the Corporation the following:

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(1) This fact found by the trial court in its opinion.

(2) This fact found by the trial court in its formal findings.

(3) For convenience called the Steel Corporation.

On October 1, 1922 (almost two years after the inception of the venture) he was credited with a dividend of $73,125: salary, September 20, 1920, $50,000: March 16, 1921, $25,000.[1]

Finding the Bardes were withdrawing funds from the venture without proper accounting, Petitioner withdrew on March 22, 1923, the Bardes purchasing his interest for $200,000.[2] (R 181, 425-6, 437, 689-94)

The aggregate of the above constitutes the proceeds of the alleged bonus paid Petitioner ($348,125) and with interest ($388,360.57) makes up the judgment of $736,485.57.

This Suit.

In October, 1932, an attorney employed by one Etienne Lang to investigate certain claims against the Bank arising out of oil transactions, called his attention to an item in a detective's report showing that Petitioner had been a partner in the steel venture with the Bardes. He advised investigating the matter because it might prove to be of assistance in the oil claims. (R 459) The investigation was made. On October 29, 1934, Lang wrote demanding that the Bank bring action against Petitioner. (R 30) On November 13, 1934, the Bank's Board of Directors adopted a resolution

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(1) The profits of the Steel venture were as follows:
1920—$95,253.28
1921—140,946.14
1922—141,807.94 (R 411)

(2) This fact found by the trial court in its opinion.

to the effect that the claim had been investigated, that it was without merit, and that no action be brought. (R 72) On December 5th this suit was filed.

Plaintiffs own, in the aggregate, 1554 shares of the stock of the Bank, out of 770,000 shares outstanding (.2 of 1%). They owned only 174 shares at the time of the transaction. (R 46, 494, 585, 132)[1]

There is no evidence that any stockholder, other than plaintiffs, favored or favors this suit.

Summary.

The following essential facts are not disputable:

1. The Bardes and Petitioner were 50-50 partners in the venture and each contributed half the capital as agreed (Bardes $500,000: Petitioner $500,000 in cash, securities or a bond as required). Each had a 50% liability for all losses, capital as well as operating.

2. Petitioner did not know the Bardes would or might want to borrow at the Bank or elsewhere; believed they had the cash: and the question of borrowing was not broached until after the partnership venture had been finally agreed upon.

3. The loans to the Bardes were authorized by the Finance Committee (Petitioner not acting) with full knowledge that the proceeds were to be used in this venture and that Petitioner was a partner therein.

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(1) The holders of these 174 shares were the only qualified plaintiffs (Eq. Rule 27, Civil Procedure Rule 23 (b)). There is no evidence of devolution by operation of law.

4. The loans were desirable loans, were secured by Liberty Bonds, were "fully protected" as found by the trial court in its opinion and were repaid in four months.

5. The loans were handled in the usual course; no customary step was omitted: Petitioner's interest in the venture was common knowledge in the Bank.

6. When the loans were made it was lawful for a National Bank President and his partners and enterprizes in which he was interested, to borrow from his bank, and such loans were ordinary and not subject to criticism; today under Act of Congress, loans may be made to a partnership in which a National Bank President does not have more than a 50% interest.

7. The plaintiff stockholders held 174 shares of stock in the Bank when the transaction took place; the inception of the suit was grounded upon their desire to develop facts helpful to them in disconnected litigation against the Bank and Petitioner; no other stockholders joined the plaintiffs.

8. Plaintiffs' demand on the Bank that it bring suit was considered and investigated by its Board of Directors, which by resolution found the claim should not be prosecuted and declined. There is no evidence whatever, and no finding, that the Bank or its Directors were ever controlled or dominated by Petitioner, or that they ever had any interest in the transaction.

9. There is no evidence whatever that the refusal of the Board of Directors to accede to the demand of Lang that suit be brought was wrongful or con-

stituted a breach of trust, or was in bad faith, or resulted from domination or control by Petitioner or others in his behalf, or was anything other than an exercise of the directors' honest discretion.

10. The trial court excluded as immaterial the evidence offered by Petitioner that the refusal of the Board of Directors to accede to Lang's demand was a free and voluntary act taken in good faith, without domination or control by Petitioner or anyone in his behalf or interests adverse to the Bank, and without any breach of trust or wrongful conduct, and in the exercise of the Board's honest discretion as to the rights and best interests of the Bank. (R 631-2, 755-60, 786-94; Assigned Error No. 7)

11. The trial court also excluded the evidence offered by Petitioner that Lang's demand for suit was made in bad faith with the object of compelling the Bank to buy its peace by settling the oil land suit which Lang and some of Respondents were then prosecuting against the Bank and Petitioner. (R 631-2, 755-60, 786-94)

12. The suit was not filed until 15 years after the transaction took place. In the interim 13 of the 19 directors then in office died; two of the four members of the Finance Committee died; other officers and employees whose testimony would have been valuable, died; records and documents are missing.

OPINIONS BELOW.

Opinion of the trial court: (R 175) 21 Fed. Supp. 527.

Opinion of the Circuit Court of Appeals: (R 900) 109 F. (2d) 543.

JURISDICTION.

The decision of the Circuit Court of Appeals was rendered February 7, 1940. A petition for rehearing was seasonably filed March 7, 1940: it was duly entertained and denied April 3, 1940. (R 933) The mandate has been stayed until July 3, 1940, and thereafter until disposition of the matter by this Court. (R 936)

The jurisdiction of this Court is invoked under Section 240(a) of the Judicial Code. (U. S. Code, Title 28, Section 347)

THE ACTION OF THE COURTS BELOW.

Contentions of the Parties.

The theory advanced by plaintiffs was that Petitioner, President of the Bank, demanded or exacted as a condition to the Bank's lending $325,000 to the Bardes, that he be given a bonus of one-half of the profits of the venture; that plaintiff stockholders had demanded the Bank file suit; that the directors refused; that they were dominated by Petitioner.

The defense was threefold:

1. That while Petitioner recommended the loans, he did not receive his interest in the steel venture for so doing, or in whole or in part for the loans, but he received it in consideration of contributing his agreed half of the partnership capital: that he did not make the loans (which had never been mentioned when the partnership was formed) on behalf of the Bank but such loans were made by the Bank's Executive Committee, with knowledge (supplied by Petitioner) that he had a half interest in the venture and that the funds were to be used therein.

2. That Equity Rule 27 and the substantive law expressed thereby, was not complied with, and plaintiffs could not maintain the action because the cause of action, if any, belonged to the Bank, and the refusal of the Board of Directors to bring suit was not wrongful, but in good faith, the Board of Directors not being interested adversely to the Bank or in the transaction or dominated or controlled by the Petitioner.

3. That the action was barred by laches and the Statute of Limitations,[1] because the delay of 15 years in filing it was unexcused; that the facts of the transaction complained of were known to the Bank

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(1) California Code of Civil Procedure §338 sub. 4 provides that an action for relief on the ground of fraud or mistake must be brought within 3 years, and that "the cause of action in such case (is) not to be deemed to have accrued until the discovery by the aggrieved party, of the facts constituting the fraud or mistake."

and its officers at the time, and great prejudice had resulted from the long delay.

The Action of the Trial Court.

1. On the merits the trial court found that although the partnership agreement was made and Petitioner had his interest therein before he knew or it was suggested that the Bardes would want to borrow, nevertheless Petitioner violated his trust to the Bank: that "a part of the consideration for the loan * * * was the participation by Herbert Fleishhacker with them in the profits of the steel deal; that Herbert Fleishhacker made a private profit for himself in the discharge of his official duties." (R 196) Although plaintiffs had charged that Petitioner had demanded that he be given a half interest in the venture in consideration of procuring the loans, there was, they admitted (R 705) and the court found, no proof of this, the court merely finding by a process of inference from the fact that the proceeds of the loans contributed to the success of the venture, that there was an implied agreement that part of the consideration for the loans was Petitioner's participation in the venture.

2. The court held that Equity Rule 27 had been complied with solely upon the grounds (a) "In acknowledging receipt of this demand (that the Bank sue), the chairman of the board stated that he would communicate with Etienne Lang later. No such communication was ever sent or received;"[1] (b) "No

(1) The demand was dated October 29, 1934; suit was filed December 5, 1934.

request was made that Lang appear and offer proof of the charges made. The board merely passed a resolution that no action be taken"; (c) "Thereafter the directors made common cause with Herbert Fleishhacker in seeking to justify his acts"; (d) "It is permissible to conclude from these facts, as said by plaintiffs' counsel, 'that the directors were either under the domination of Fleishhacker or saw fit to accept his denial of wrongdoing.'" (R 195-6)[1]

The trial court made no mention of its refusal to permit Petitioner to introduce evidence to show the reasons for the Bank's refusal to sue.

3. The trial court held the action was not barred by laches or the Statute of Limitations because "* * * while the officers of the Anglo knew of the transaction, it was not at that time known to plaintiff stockholders. Besides the question of secrecy is immaterial" (R 191); that the plaintiff stockholders did not discover the facts until 1933, and since suit was filed in 1934, it was filed in time. (R 196)

We urge a reading of the opinion of the trial court (R 175), which contains a recital of the facts with which Petitioner in the main agrees (although some important facts are omitted and erroneous inferences

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(1) Judge Mathews in his dissenting opinion in the court below (R 922) pointed out that these circumstances which formed the sole basis for the trial court's conclusion on this point constitute no sufficient showing to enable plaintiffs to maintan the suit and said "I find here a total lack of any factual showing entitling appellees to maintain this suit". (R 920)

are drawn) and which shows clearly the basis for that court's decision.

The Action of the Circuit Court of Appeals.

On appeal, among other points, Petitioner urged:

1. That on the face of the trial court's opinion and findings, it was impossible to infer the existence of an agreement for a bonus, because the court found that the partnership agreement was made before it was even suggested that the Bardes would or might want to borrow.

2. That on the face of the trial court's opinion and findings, Equity Rule 27 had not been complied with because there was no allegation, no evidence and no finding, that the Directors, in refusing to bring suit, had committed a breach of trust; hence plaintiff stockholders were not entitled to assert a cause of action which, if it existed at all, belonged to the Bank and not to its stockholders.

3. That on the face of the opinion and the findings of the lower court (finding expressly that the officers of the Bank knew of Petitioner's interest in the transaction at the time), the action was barred by laches and the Statute of Limitations.

The decision of the trial court was affirmed as against Petitioner by a divided court.

The majority (Judges Healy and Stephens) sustained the trial court's decision by the following process of reasoning (R 900):

1. On the merits, the court below accepted the trial court's finding that Petitioner did not learn of the Bardes' desire to borrow until after the parties had entered into the partnership agreement, namely that $1,000,000 of capital would be required; that the Bardes would supply half, in cash if required, that the Petitioner would supply the remaining half, in cash, securities, or a bond, as required by the Shipping Board, and that each would have a half interest.

But the court rejected (by ignoring it) the trial court's reasoning, and substituted therefor its own contradictory inferences of fact and legal conclusions. It found (a) that the original partnership proposal was made by the Bardes with the undisclosed intention of later requesting loans from the Bank (this proposition is original with the court; it is not suggested in the evidence, in the argument or briefs, or in the trial court's opinion or findings); (b) that after the parties had investigated the matter and agreed to proceed, the Bardes disclosed their desire to borrow, and requested a loan from the Bank; (c) that although the parties had agreed on the terms of the partnership, as outlined above, before the Bardes disclosed their desire to borrow, nevertheless the partnership agreement was still "at large", because, as it held, "the details were uncertain," (the trial court had no such idea and found to the contrary).

Having drawn these inferences of fact, the court concluded that Petitioner by continuing with the venture after the Bardes expressed their desire to borrow,

may be said to have agreed that the loans would be procured in consideration of his interest in the partnership.

2. As to Equity Rule 27, the majority, after pointing out that the complaint did not allege in so many words that the Directors' refusal to sue constituted a breach of trust, or was wrongful or improper, and that the trial court made no specific finding to that effect, nevertheless concluded that "It is obvious from the findings as a whole as well as from the opinion, that the court looked upon the Board's refusal to sue as amounting to a breach of trust". (R 911) No mention is made of the fact that there was no evidence to sustain such view, or of the refusal of the trial court to admit evidence offered by Petitioner to show the reasons for the Board's action and that it acted honestly and committed no breach of duty.

3. As to laches and the Statute of Limitations, the majority exhibited awareness that the trial court erred in holding that the Bank's knowledge of the alleged fraud was irrelevant, but it avoided the difficulty by contradicting the trial court's finding that the Bank had knowledge thereof in 1919.

The court below reached its conclusion that the action was not barred by laches or the Statute of Limitations by (a) summarizing the evidence which defendants had offered to show that all the essential facts of the alleged fraud were known, as a result of Petitioner's disclosure, to numerous officers of the Bank in 1919; (b) concluding (contrary to the trial

court) that that evidence was insufficient to prove that the Bank had notice in 1919; and (c) then finding on the basis of that same evidence alone, "that the proof is such as to require a finding that the Bank did not discover the fraud until appellees brought it to light [in 1933] by their investigations. Hence the action is not barred as to the Bank." (R 912)

The court failed to see that what was known in 1919 could not possibly sustain the burden of showing that no discovery was made in the 15 following years which passed before the suit was filed.

Judge Mathews in his dissenting opinion (R 915) demonstrated the "total lack of any factual showing entitling appellees to maintain this suit. There was neither allegation nor proof that Anglo's board of directors had done or threatened to do any act which was beyond the authority conferred on them by their charter or other source of organization; or that any fraudulent transaction had been completed or contemplated by the board of directors; or that the board, or a majority of them, were acting for their own interest, in a manner destructive of Anglo, or of the rights of other stockholders; or that a majority of Anglo's stockholders were oppressively and illegally pursuing a course, in the name of Anglo, which was in violation of the rights of other stockholders; or that irremediable injury would be suffered, or that a total failure of justice would occur, if the court did not exercise its preventive powers." (R 920)

He concluded that the decree should be reversed with directions to dismiss the bill of complaint.

Questions Presented.

The questions here may be summarized as follows:

1. Did the court below err (as Petitioner contends) in holding that this stockholder's derivative suit could be maintained under Equity Rule 27 (now Civil Procedure Rule 23), notwithstanding a failure by such stockholders to show either that the Directors' refusal to sue constituted a breach of trust or was wrongful or improper, or that the Bank or its Board of Directors is or ever was dominated or controlled by defendant? (See dissenting opinion in the court below, R 915.)

2. Did the court below err (as Petitioner contends) in failing to hold that the trial court committed error in excluding Petitioner's evidence offered to show (a) the investigation made by the Bank concerning the demand that it bring suit; (b) the reasons which impelled the Board of Directors to adopt a resolution not to bring suit; and (c) that this suit was brought for ulterior reasons, namely, to force settlement of a wholly unrelated controversy?

3. Did the court below err (as Petitioner contends) in failing to hold that this suit was barred by laches and by the Statute of Limitations because in the bill charging a fraud committed 15 years before suit was brought, no attempt was made to show that the Bank did not know the facts of the alleged fraud from the beginning, and where (although admittedly the burden was on plaintiffs to show the Bank did not have notice and to excuse the Bank's delay of 15

years before suit brought), no evidence was offered concerning what was known or became known to the Bank at any time thereafter?

4. Did the trial court violate an important principle of judicial administration (as Petitioner contends) in signing the findings prepared by the successful party without change, although they contradict that court's own view of the facts (as expressed in its opinion which it ordered the findings should follow) in several important particulars, and are in numerous respects contrary to the evidence?

5. Did the court below err (as Petitioner contends) in affirming the decision of the trial court (which was based on a palpably erroneous theory of law), by adopting a view of the facts which (we submit) contradicts the opinion and findings of the trial court and the evidence and admissions of plaintiffs' counsel?

6. Did the court below err (as Petitioner contends) in failing to find that Petitioner did not receive a bribe or bonus for procuring a loan of the Bank's funds, and in failing to find that he did not commit any breach of his fiduciary duty to the Bank?

REASONS FOR ALLOWANCE OF WRIT.

1. The Court below has Decided a Federal Question in a Way Conflicting with Applicable Decisions of this Court.

Federal Equity Rule 27 (Civil Procedure Rule 23-B) not only states a requirement of pro-

cedure, but a principle of substantive law, i.e., that a cause of action belonging to a corporation may not be asserted or enforced by a stockholder unless it is affirmatively shown (a) that upon demand the Board of Directors refused to bring suit (or that such demand would be unavailing); and (b) that the refusal of the Directors to bring suit constituted a breach of trust or that it was wrongful or improper. These principles have been recognized and endorsed in a long line of decisions of this Court beginning with *Hawes v. Oakland* (1882) 104 U. S. 450[1] which indeed was the inspiration for old Equity Rule 94, the predecessor of Rule 27.

The complaint alleged in this behalf that the Board of Directors was dominated by Petitioner. This was denied, no evidence was produced to sustain it and the trial court made no finding thereon. The attempt of the court below to repair this error by a general statement that it was satisfied "that the Appellants had the right to bring suit" is merely to declare in substance that whenever a board of directors refuses to bring suit on demand, then a stockholder may, without more, bring suit on the corporation's alleged cause of action.

As shown by the dissenting opinion, the rule announced below is in conflict with applicable decisions

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(1) *Corbus v. Alaska Treadwell Gold Mining Co.*, 187 U. S. 455; *United Copper Securities Co. v. Amalgamated Copper Co.*, 244 U. S. 261; *Ashwander v. Tenn. Valley Authority*, 297 U. S. 288.

of this Court and opens the federal courts to any stockholder who (whether in good faith or bad) seeks to substitute his judgment on questions of managerial policy for that of the board of directors, enabling him to compel and conduct litigation of the corporation's claims, real or false, even though the directors are disinterested, and, in the exercise of an honest discretion as to the rights and best interests of the corporation, believe it should not be done.

The rule thus announced not only destroys the principle that the directors, not individual stockholders, should decide questions of management, but goes further, and makes the federal courts the agency for destroying that principle (since virtually all state courts, including California, hold the contrary).

This, we submit, is at variance with the applicable decisions of this Court, as well as Equity Rule 27 and Civil Procedure Rule 23B, and we may add with the decisions of the Supreme Court of California (*Waymire v. San Francisco Railway,* 112 Cal. 646, 649, and cases cited in the attached brief).

The decision of the court below, unless reversed, will be cited (in addition to a holding that no wrongful refusal need be shown) as authority for the proposition, and has already been digested and reported in the National Reporter System as establishing the rule that:

> "In derivative suit by national bank stockholders to recover amounts received by bank president for arranging bank loan, complaint,

alleging demand upon bank's board of directors to bring action and their refusal to bring it, *held* sufficient under equity rule requiring complaint to set forth with particularity plaintiff's failure to secure action by managing directors or trustees. Equity Rules, rule 27, 28 U. S. C. A. following section 723; Rules of Civil Procedure for District Courts, rule 23(b), 28 U. S. C. A. following section 723c."

Fleishhacker v. Blum, 109 Fed. (2d) 543, headnote 6.

The error just described is emphasized by the fact that the trial court refused to permit Petitioner to introduce evidence offered to show: (a) The results of the investigation made by the Bank in considering the demand that it bring suit on the claim here involved; (b) The reasons which impelled the Board of Directors to adopt a resolution not to bring the suit; (c) That the Board did not refuse wrongfully or violate its trust in so refusing, and that it acted without adverse interest or domination or control by Petitioner or others; (d) That this suit was brought for ulterior reasons, namely, to force settlement of a wholly unrelated claim against the Bank.

Moreover, the decision excluding this evidence, opens the federal courts to collusive suits wherein no true diversity of citizenship exists:[1] this because, if (as

(1) Here both Petitioner and the Bank are citizens of California, and the basis of federal jurisdiction is diversity. (R 293-94)

held here) such reasons are immaterial as a matter of substantive law, then no inquiry may be had.

2. The Court below has Decided an Important Question of Law in a Way Conflicting with Applicable Local Decisions, as well as Decisions of this Court, and has Applied the Rule of Laches and the Statute of Limitations in such a Way as to Open the Federal Courts to Unlimited Speculation in Stale Charges of Fraud.

In California actions of this character are governed by Section 338 subdivision 4 of the Code of Civil Procedure, which provides that actions for relief on the ground of fraud or mistake must be brought within three years and that "the cause of action in such case (is) not to be deemed to have accrued until the discovery, by the aggrieved party, of the facts constituting the fraud or mistake."

The California decisions uniformly require both at law and in equity that when a complaint shows on its face that the action has been filed beyond the statutory period of three years, there must be specific allegations excusing the delay by showing that the facts constituting the fraud or mistake were not discovered by the aggrieved party until within the statutory period, and further that these allegations must be proved. (*Earl v. Lofquist,* 135 Cal. App. 373; *Lady Washington Co. v. Wood,* 113 Cal. 482; *Pourroy v. Gardner,* 122 Cal. App. 521; *Consolidated Reservoir*

& Power Co. v. Scarborough, 216 Cal. 698.) The decisions of this court establish the same rule (*Wood v. Carpenter,* 101 U. S. 135) and point out that in cases of this kind, the complainant is held to stringent rules of pleading and evidence.

Here the aggrieved party was the Bank. (*People v. Noyo Lumber Co.,* 99 Cal. 456; 16 Cal. Juris. pp. 503, 504.) The action was filed 15 years after the alleged cause of action arose. The complaint contains no allegations whatever directed to showing the Bank did not have knowledge until within three years of the filing of the action or that the Bank was adversely dominated or controlled during the period of delay, or even attempting to excuse its failure to file suit within the statutory period. There is no evidence excusing such delay. The court failed to find any facts excusing such delay.

There was therefore complete failure here to comply with either the California law or the Federal law.

But the error goes deeper, for not only did the plaintiffs fail in their burden of proving lack of notice, but the trial court actually found that the Bank had notice at the time. This compelled a finding that the action was barred, but the court made no such finding because of its erroneous conception that the stockholders and not the Bank were the aggrieved parties.

The court below, after pointing out that the plaintiffs failed to make the necessary allegation, and the

court failed to make the necessary finding,[1] erroneously proceeded to supply this essential and contradictory finding.

But although the court below admitted that "the burden of proving lack of discovery by the Bank rested upon appellees" (R 914), it nevertheless rested its finding that the Bank did not have notice, on evidence which Petitioner introduced to show affirmatively that the Bank did have notice at the very time of the transaction, i. e., 15 years before suit brought. In short the court not only used evidence of what Petitioner disclosed at the time the loans were made as proof that the Bank did not know all of the essential facts at that time, but went further and held this same evidence (there being no other) sufficient to sustain the plaintiffs' admitted burden of proving that at no time during the many years that followed did the Bank's officers know, or discover, or have reason to suspect, anything beyond what they are shown to have known in 1919. (This was also contrary to the California and Federal rule requiring, in the absence of any evidence, a finding against the party having the burden of proof. *Golson v. Dunlap,* 73 Cal. 157, 161; 24 Cal. Juris. 937-8.)

Whether the rule to be applied is laches or the Statute of Limitations, the result is the same. The decision of the court below opens the federal courts

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(1) As pointed out in the accompanying brief, the trial court (contrary to the statement of the court below) actually found that the officers of the Bank had knowledge of the facts at the time. (R 190, 191, 313)

to unlimited speculation in stale charges of fraud, and is contrary to the applicable local decisions and the decisions of this Court.

3. The Court below has Departed from the Accepted and Usual Course of Judicial Proceedings and has Sanctioned such a Departure by the Trial Court.

The formal findings in the trial court were prepared by plaintiffs' counsel and were signed without alteration by the trial judge. (R 766) They depart in numerous important particulars from the trial court's opinion (which the trial court ordered they should be in accordance with (R 197)) and in many essentials are unsupported by or contrary to the evidence. These findings were used by the court below as the basis of its decision; but it went further, and upon concluding that the trial court had failed to find on essential issues, itself relied on findings imported by plaintiffs' attorney, and supplied the necessary findings by drawing inferences from the findings so prepared; and supplied other findings (also drawn by inference from the findings so prepared) at variance with those of the trial court.

The accepted and usual course in such cases, and that contemplated by the Rules of Civil Procedure is that the findings shall be prepared by the trial judge, or, if prepared by counsel, shall accurately reflect the court's view of the facts. See *Process Engineers v. Container Corp.*, 70 F. (2d) 487; *Brenger v. Brenger*, 142 Wis. 26; *Nashville Ry. Co. v. Price*, 125 Tenn. 646.

It is further the accepted and usual course when the trial court has failed to find upon an essential

issue or has misconceived the applicable law that the case should be reversed with directions to dismiss or sent back for further proceedings in the trial court. See *Indiana Farmers Guide Pub. Co. v. Prairie Publishing Co.*, 293 U. S. 268, 281.

4. The Court below Erred in Finding that Petitioner Received a Bonus for a Loan of the Bank's Funds and Received a Profit for which he Must Account to the Bank.

This is not a case in which the "two court" rule as to findings of fact is applicable; essential findings of the trial court and the court below are contradictory.

The evidence shows without contradiction that Petitioner received his interest in the partnership venture in consideration of his contribution of half its capital, and not as a consideration for the Bank loan; that he had such partnership interest before the loan was even thought of; that the loan was made in behalf of the Bank, not by Petitioner, but by its Finance Committee, with knowledge of Petitioner's interest supplied by Petitioner: that the loan was a desirable one, secured by Liberty Bonds, and was repaid in four months: and that there was no secrecy.

These being the facts, and having in mind that when these loans were made a national bank president, his partners, and an enterprise in which he was personally interested, could borrow from his bank;[1] that

(1) *National Bk. Commerce v. National Bank of Missouri*, 30 Fed. Cas. 1121, 1122; *Blair v. First National Bank*, 3 Fed. Cas. 577, 580; *Gallin v. National City Bank*, 273 N. Y. S. 87, 97; 7 *Michie, Banks and Banking* (Perm. Ed.) p. 270; 1 Michie op. cit., p. 145.

a partnership or corporation in which he has a 50% interest, may now, under affirmative Act of Congress, borrow from such bank;[1] that it is not a breach of trust for a bank president to recommend a bank loan to be used in a venture in which he has an interest, provided the loan is properly safeguarded, and his interest is known to those who make the loan in behalf of the Bank, as was the case here: that fraud is never presumed and the presumption against it approximates that of innocence of crime: that if an inference of fair dealing can as readily be drawn as an inference of corrupt practice, then it is the express duty of the court to draw the inference of fair dealing, it seems inconceivable that 19 years after the transaction, a judgment for almost $800,000 should be rendered against Petitioner, whose affairs are now in the bankruptcy court. Particularly is this so where the suit was filed 15 years after the event by stockholders whose inspiration was a desire to obtain evidence to be used in other litigation adverse to the Bank, and where the ultimate finding of fraud and crime was based solely on inference and conjecture.

WHEREFORE, Petitioner prays that a Writ of Certiorari be issued out of and under the seal of this Hon-

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(1) 12 U. S. C. §375a (Banking Act of 1933, chap. 89, §12, 48 Stat. 182, as amended June 14, 1935, 49 Stat. 375; Aug. 23, 1935, 49 Stat. 716; April 25, 1938, 52 Stat. 223; June 20, 1939, 53 Stat. 842). cf. Rulings of Federal Reserve Board, Fed. Res. Bulletins, April 1936, pp. 249 and 250; Proceedings Subcommittee Banking and Currency Committee, U. S. Senate, 74th Congress, 1st Session, pp. 79-100.

orable Court directed to the United States Circuit Court of Appeals for the Ninth Circuit, commanding that court to certify and to send to this Court for its review and determination, a full and complete transcript of the record and of the proceedings of said court in the case numbered and entitled in its docket as "No. 9021, Herbert Fleishhacker, Harry T. Thompson, Victor Klinker, Palo Alto Stock Farms, Inc., a corporation, and The Anglo-California National Bank of San Francisco, a national banking association, Appellants, vs. Lucien Blum, Edmond Lang, Elizabeth Lang, Rene Fould, Esther Fould, Max Lazard, Roger Haas, Andre Haas, Lucie Emile Lewylier, S. A. Johanesson, G. O. Hoffman, and Henry Leon, Appellees", and that the decree of said court be reversed by this Court with directions to dismiss the bill, and for such further relief as to this Court may seem proper.

Dated: San Francisco, California, June 21, 1940.

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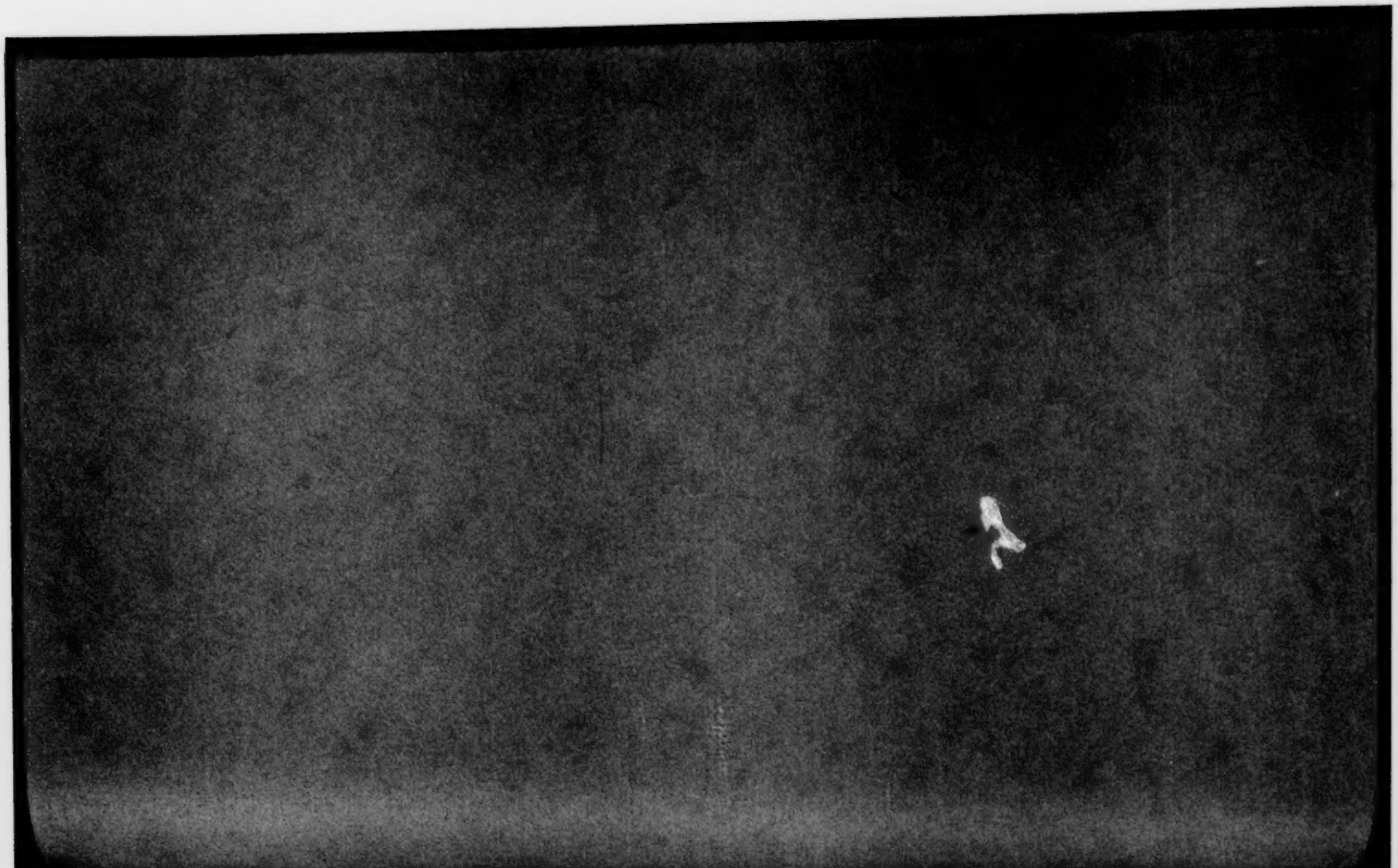

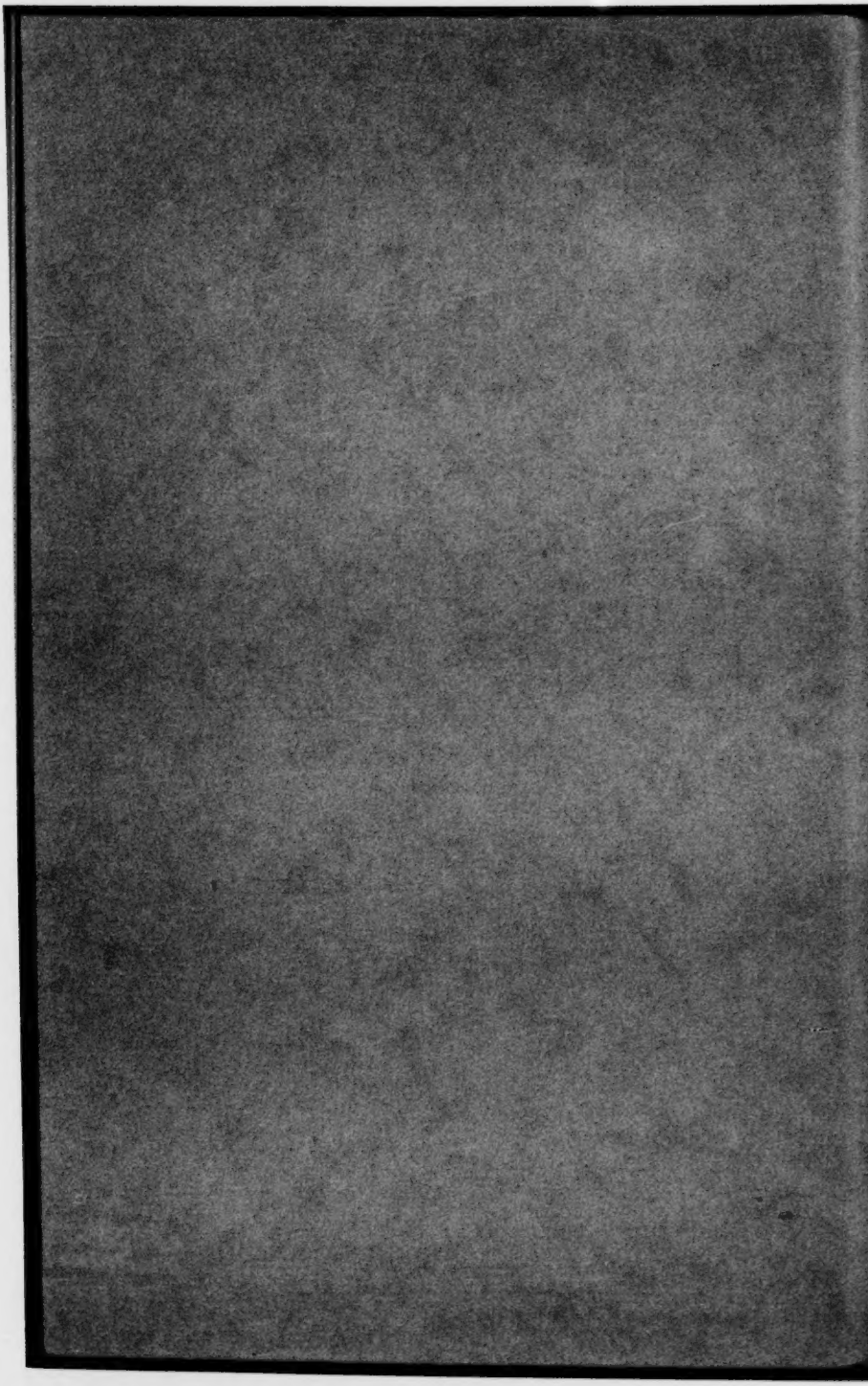

In the Supreme Court of the United States

OCTOBER TERM, 1939

No.....

HERBERT FLEISHHACKER,
Petitioner,

vs.

LUCIEN BLUM, EDMOND LANG, ELIZABETH LANG, RENE FOULD, ESTHER FOULD, MAX LAZARD, ROGER HAAS, ANDRE HAAS, LUCIE EMILE LEWYLIER, S. A. JOHANESSON, G. O. HOFFMAN and HENRY LEON,
Respondents.

Brief In Support of Petition for Writ of Certiorari.

POINT I

PLAINTIFFS FAILED TO COMPLY WITH EQUITY RULE 27; AND THE COURT BELOW, BY CONDONING PLAINTIFFS' FAILURE, EMASCULATES THE RULE.

If the decision in the court below concerning the requirements of Equity Rule 27 (now Rule 23(b), Federal Rules of Civil Procedure) is allowed to stand,

then the diversity jurisdiction of the federal courts is open to any stockholder who seeks to have his judgment on questions of managerial policy substituted for that of the Board of Directors, enabling him to compel litigation of the corporation's claims, real or false, even though the Directors decide, for the best of reasons and without breach of trust, it should not be done, and even though all of the other stockholders are in agreement with the Board.

The dissenting opinion of Circuit Judge Mathews in the court below is a clear demonstration of the fact that plaintiffs failed to comply with Equity Rule 27; and that the majority of the court below, by condoning plaintiffs' failure, emasculate both the rule and the substantive principles which it embodies.

Plaintiffs alleged a demand on the Board of Directors to bring this action, and the Board's failure to do so.

But the rule also requires that the Bill:[1]

> "Must also set forth with particularity the efforts of the plaintiff to secure such action as he desires on the part of the managing directors or trustees, and, if necessary, of the shareholders, and the causes of his failure to obtain such action, * * *."

Plaintiffs' only attempt to meet this requirement consists of the following allegation:

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(1) Federal Rules of Civil Procedure, Rule 23(b), is substantially identical.

> "Plaintiffs are informed and believe and so allege that the causes for such failure of the Board of Directors to institute an action to recover these profits are that the Board of Directors is composed of relatives, close friends and business associates of the defendant Fleishhacker and are under the domination of the defendant Fleishhacker." (R 17)

But as stated in the dissenting opinion below:

> "This allegation was denied and not proved. * * * There is no evidence that any member of the Board was dominated by Fleishhacker. Only one relative of Fleishhacker was shown to be a member of the Board." (R 922)[1]

The following quotation from the dissenting opinion of Circuit Judge Mathews sums up, we submit, the conclusion to be drawn from the foregoing:

> "The board may, in good faith, have believed that the charges made in the letter were false and unfounded; that Anglo had, in fact, no right of action against Fleishhacker, Klinker, Thompson or Stock Farms; and that it could not, in equity or good conscience, bring suit against them, or leave appellees' suit undefended. Lacking proof to the contrary, we should—and I do—presume that the board acted in good faith. Corbus v. Alaska Treadwell Gold Mining Co., 187 U. S. 455, 463.

(1) The Bank had a board of 19 members at the time of the transactions in 1919. (R 599) There is no other evidence as to the personnel of the board, their number or identity or relationships, at the time of the demand.

"Even if the board had believed that Anglo had a right of action, it might, also, in good faith, have believed that it was not to Anglo's best interest to bring suit thereon and, so believing, might properly have waived such right of action. Hawes v. Oakland, supra, 104 U. S. p. 462; Corbus v. Alaska Treadwell Gold Mining Co., supra; United Copper Securities Co. v. Amalgamated Copper Co., 244 U. S. 261, 263, 264.

"Having failed to show that the board's failure to sue constituted a fraud or breach of trust, or that it was in any respect wrongful or improper, appellees had, and have, no standing to maintain this suit.

"The decree should be reversed and the case should be remanded with directions to dismiss the bill of complaint." (R 923)

The Decision is Directly Contrary to the Decisions of This Court and of Courts Generally Including California.

This Court has laid down the rule that the power and duty of management of a corporation is vested in the board of directors; and absent fraud, bad faith or illegality, the courts will not permit (much less enable) a stockholder to insist that his judgment, rather than the board's, shall dictate the corporation's course of action.

The leading case is *Hawes v. Oakland,* 104 U. S. 450.

The authorities in general are collected in

13 Fletcher, *Cyc. of Corporations* (Perm. Ed.) Secs. 5969, 5822.

As stated by Mr. Justice Brandeis in *Ashwander v. Tennessee Valley Authority,* 297 U. S. 288, 343, in his concurring opinion joined in by Mr. Justice Stone, Mr. Justice Roberts and Mr. Justice Cardozo:

> "Within recognized limits, stockholders may invoke the judicial remedy to enjoin acts of the management which threaten their property interest. But they cannot secure the aid of a court to correct what appear to them to be mistakes of judgment on the part of the officers. Courts may not interfere with the management of the corporation, unless there is bad faith, disregard of the relative rights of its members, or other action seriously threatening their property rights. This rule applies whether the mistake is due to error of fact or of law, or merely to bad business judgment. It applies, among other things, where the mistake alleged is the refusal to assert a seemingly clear cause of action, or the compromise of it. United Copper Securities Co. v. Amalgamated Copper Co., 244 U. S. 261, 263-264. If a stockholder could compel the officers to enforce every legal right, courts, instead of chosen officers, would be the arbiters of the corporation's fate."

The case of *Corbus v. Alaska Treadwell Gold Mining Co.,* 187 U. S. 455, was, as here, a stockholder's suit by the holder of a very small proportion of stock. This Court pointed out the small interest of plaintiff, noted also that the other stockholders had not shown any interest in the alleged wrong, and spoke as fol-

lows (p. 463), concerning Equity Rule 94, the predecessor of Equity Rule 27 and the present Rule 23(b):

> "It must not be understood that a mere technical compliance with the foregoing rule is sufficient and precludes all inquiry as to the right of the stockholder to maintain a bill against the corporation. This court will examine the bill in its entirety and determine whether, under all the circumstances, the plaintiff has made such a showing of wrong on the part of the corporation or its officers and injury to himself as will justify the suit. The directors represent all the stockholders and are presumed to act honestly and according to their best judgment for the interests of all. Their judgment as to any matter lawfully confided to their discretion may not lightly be challenged by any stockholder or at his instance submitted for review to a court of equity. The directors may sometimes properly waive a legal right vested in the corporation in the belief that its best interests will be promoted by not insisting on such right. They may regard the expense of enforcing the right or the furtherance of the general business of the corporation in determining whether to waive or insist upon the right. And a court of equity may not be called upon at the appeal of any single stockholder to compel the directors or the corporation to enforce every right which it may possess, irrespective of other considerations. It is not a trifling thing for a stockholder to attempt to coerce the directors of a corporation to an act which their judgment does not approve, or to substitute his judgment for theirs."

And this Court said in

United Copper Securities Co. v. Amalgamated Copper Co., 244 U. S. 261, at 263-4:

"Whether or not a corporation shall seek to enforce in the courts a cause of action for damages is, like other business questions, ordinarily a matter of internal management and is left to the discretion of the directors, in the absence of instruction by vote of the stockholders. Courts interfere seldom to control such discretion *intra vires* the corporation, except where the directors are guilty of misconduct equivalent to a breach of trust, or where they stand in a dual relation which prevents an unprejudiced exercise of judgment; and, as a rule, only after application to the stockholders, unless it appears that there was no opportunity for such application, that such application would be futile (as where the wrongdoers control the corporation), or that the delay involved would defeat recovery. In the instant case there is no allegation that the United Copper Company is in the control of the alleged wrongdoers or that its directors stand in any relations to them or that they have been guilty of any misconduct whatsoever. Nor is there even an allegation that their action in refusing to bring such suit is unwise. No application appears to have been made to the stockholders as a body or indeed to any other stockholders individually; nor does it appear that there was no opportunity to make it, and no special facts are shown which render such application unnecessary. For aught that appears, the course pursued by the directors has the approval of all the stockholders except the plaintiffs."

The California rule is the same. Thus in *Waymire v. San Francisco etc. Ry. Co.,* 112 Cal. 646, 649, the Supreme Court of California said:

> "Therefore, as a general rule, the action should have been brought by and in the name of the corporation; but when, upon proper demand by stockholders, the corporation *wrongfully* refuses to institute an appropriate action, or when it appears that such demand by stockholders would have been unavailing and fruitless, an action may be instituted and prosecuted by a stockholder for the direct and immediate benefit of the corporation, and for the incidental benefit of the stockholders."

The italics in the above quotation are the court's. Again, in

> *Thomson v. Mortgage Investment Co.,* 99 Cal. App. 205, 215,

the court said:

> "* * * such actions may be instituted and maintained by stockholders only when the acts of the board of directors of the corporation are either *ultra vires,* illegal, fraudulent, oppressive or show wilful neglect. (Fletcher's Cyclopedia of Law of Private Corporations, sec. 4065; Hawes v. Oakland, 104 U. S. 450. * * *)"

See, also, *Difani v. Riverside County Oil Co.,* 201 Cal. 210, 215 and cases cited; *Whitten v. Dabney,* 171 Cal. 621, 630; *Cogswell v. Bull,* 39 Cal. 320, 324.

But the court below has announced and applied a very different rule; namely, that any stockholder who

chooses to, may demand that the corporation bring an action and, if refused, may, without either pleading or proof that the corporation's refusal to sue was wrongful, maintain the action on its behalf, even though the board of directors believes and decides, and even though it is a fact, that prosecution of the action is unwise or will be unjust, or futile, or harmful to the corporation.

The Opportunities for Misuse of Stockholders' Suits Are Unlimited Under the Rule Announced Below.

Equity's allowance of suits by stockholders is necessary to avoid injustice, but dangerous, because of the misuse of such suits by misguided or meddlesome dissenters, and as indirect means of extortion or coercion. See the many references under Rule 23(b) in Moore's Federal Practice, Vol. 2, pp. 2246-76.

See, also, an excellent note, *"Extortionate Corporate Litigation"*, 34 Columbia Law Review, 1308.

See, also, *"A History of The Libel Suit of Clarence H. Venner against August Belmont"* (1913).

The court below, without adding anything to the value of stockholders' suits, makes them a perfect instrument for the accomplishment, by indirection, of wholly illegitimate ends.

Federal Diversity Jurisdiction Can Be Manufactured Almost at Will Under the Rule Announced Below.

Any dissident stockholder or group who can find a non-resident stockholder willing to act as plaintiff,

can thereby create federal diversity jurisdiction of any suit such as this.

If, as held below, any stockholder may bring suit on any real or pretended cause of action which the corporation refuses (for the best of reasons) to prosecute, then this source of litigation in the federal courts is enormously enlarged.

The rule announced below, therefore, not only destroys the principle that the directors and not individual stockholders should decide questions of management, but makes the federal courts the agency for destroying that principle (since virtually all states hold the contrary), and invites a great and uncontrolled expansion of such misuse of the federal courts. Here both Petitioner and the Bank are citizens of California.

Petitioner Was Not Allowed to Show the Reasons for the Bank's Refusal to Bring This Suit.

The error just discussed is emphasized by the fact that the trial court excluded Petitioner's evidence offered to show why the Board of Directors of the Bank refused to bring this suit. (R 630-32, 786) In the assignment of error on this point the substance of the evidence thus excluded is summarized as follows (R 786, 792-94):

> "The substance of the evidence which defendant would have introduced but for said exclusion by the Court is as follows:

"The Board of Directors had knowledge of the transactions complained of in the Bill of Complaint, and had made an independent investigation of same prior to its receipt of the demand of Etienne Lang; and upon receipt of said demand again investigated and reviewed the same.

"The investigation made by the Board resulted in the ascertainment by it of the following facts:

"a. That the Bank had knowledge of said transactions in December 1919 and January 1920, when said loans were made, and at all subsequent times.

"b. That the Bank had knowledge in December 1919 of the personal interest of defendant Herbert Fleishhacker in the steel venture in which the proceeds of the loans were employed and of his hope to make a personal profit therefrom, which facts were disclosed to it by said defendant.

"c. That the Bank at and from the time of said transactions consented to the participation of defendant Herbert Fleishhacker in the said venture and to the receipt and retention by said defendant of the profit therefrom.

"d. That the Board of Directors had knowledge of all of the facts as to the activities of Lang which were later revealed at the trial.

"e. That the demand was not made in good faith, but was made for the purpose of injuring the Bank, and aiding the members of the Lazard family (represented by Lang) in other litigation in which large sums of money were demanded for alleged frauds by the Bank and its chief executive officer.

> "The Board concluded after such investigation, that the Bank did not have any valid, legal or equitable claim as a result of said transaction, and that the institution of suit thereon would injure the Bank.
>
> "The members of the Board at all said times were independent of defendant Herbert Fleishhacker, and were not dominated or controlled by him and had no adverse interest to the Bank."

The view entertained below is thus made clear: Although a corporation refuses to bring suit in entire good faith, and for the best of reasons, and all but one stockholder agree, nevertheless, that one stockholder may compel complete litigation of the corporation's alleged claim by proceeding in the federal courts, provided only that diversity of citizenship between the complaining stockholder and the real defendant can be shown.

It is unnecessary to labor the point that the trial court's exclusion of Petitioner's evidence offered to show the Board of Directors' investigation of plaintiff's demand to sue, the results of that investigation, and the reasons which impelled the Board (acting without domination or adverse control) to refuse the demand, was prejudicial error. This because, as the authorities abundantly show, the ultimate question as to the right of a stockholder to sue on behalf of a corporation is whether or not the refusal of the corporation itself to sue was wrongful.

Moreover, the decision of the inferior courts excluding as immaterial as a matter of substantive law the reasons why the Board of Directors refused to

bring suit, directly opens the federal courts to collusive suits wherein no true diversity of citizenship exists: this because, if such reasons are immaterial as a matter of substantive law, then whether they be valid or the result of collusion to create a false diversity of citizenship, no inquiry as to those facts may be had.

Plaintiffs' Interest in the Bank Is Slight; No Other Stockholders Complain.

Plaintiffs own in the aggregate 1554 shares of the stock of the Bank out of 770,000 shares outstanding. (R 44-5, 132) Plaintiffs, therefore, own about 2/10ths of 1% of the outstanding stock in the Bank. And they only owned 174 shares at the time (1919) of the acts complained of. Their respective holdings, and their respective monetary interest in the judgment recovered, are as follows (R 44-45, 132):

	Shares	*Date Acquired*[1]	*Interest in recovery.*
Rene Fould and Esther Fould	8	April 1, 1909	$ 7.68
Edmond Lang and Elizabeth Lang	2	April 1, 1909	1.92
S. A. Johanesson	12	October 28, 1918	11.52
Lucien Blum	128	March 25, 1910	122.88
Max Lazard	8	April 1, 1909	7.68
G. O. Hoffman	16	October 28, 1918	15.36
Henry Leon	248	April 7, 1922	238.08
Roger Haas	416	November 27, 1928	399.36
Andre Haas	416	November 27, 1928	399.36
Lucie Emile Lewylier	300	July 12, 1932	288.00

(1) There is absolutely no evidence to support the finding that Henry Leon was a stockholder at all times mentioned in the Bill (R 295) or the finding that the stock of Roger Haas, Andre Haas, and Lucie Emile Lewylier devolved on them by operation of law. (R 312)

The relatively microscopic interest of the plaintiffs in the subject-matter of this suit, and the fact that so far as appears all of the other stockholders in the Bank were and are entirely satisfied with the course taken by the directors are plainly persuasive evidence, (a) that the claim is in fact without foundation, and (b) that the Board of Directors' decision not to sue was a proper exercise of the Board's discretion. The authorities make this clear. See *Corbus v. Alaska, etc. Gold Mining Co.,* 187 U. S. 455, 463; *United Copper Securities Co. v. Amalgamated Copper Co.,* 244 U. S. 261, 263-4; *Carson v. Allegany etc. Co.,* 189 Fed. 791; *Presidio Mining Co. v. Overton,* 261 Fed. 933, 940.

POINT II

THE ACTION IS BARRED BY LACHES AND THE STATUTE OF LIMITATIONS

If a suit brought by the Bank itself would have been barred by laches or the statute of limitations, then, of course, this stockholders' suit, brought on behalf of the Bank, is likewise so barred.

13 Fletcher, *Cyc. of Corporations* (Perm ed.) Sec. 5947;
Earl v. Lofquist, 135 Cal. App. 373, 376-8.

The Bank is the "aggrieved party" under the California Statute of Limitations. (*People v. Noyo Lumber Co.,* 99 Cal. 456, 461; 16 Cal. Juris. 503-4).

It follows that the plaintiff must show that the corporation's right to sue has not been lost; and in

this behalf must plead and prove facts which excuse the corporation's fifteen-year delay in asserting the cause of action put forward on its behalf.

> 13 Fletcher, *Cyc. of Corporations* (Perm. ed.) Sec. 6005.

Of the almost countless cases laying down the detailed and convincing proof required of plaintiffs seeking to escape from laches or the statute of limitations, in a suit based upon a claim of fraud, where (as here) the events constituting the alleged cause of action took place many years before suit was brought, one of the most important is *Wood v. Carpenter,* 101 U. S. 135. In that case this Court said in part (140):

> "In this class of cases the plaintiff is held to stringent rules of pleading and evidence, 'And especially must there be distinct averments as to the time when the fraud, mistake, concealment, or misrepresentation was discovered, and what the discovery is, so that the court may clearly see whether, by ordinary diligence, the discovery might not have been before made.' Stearns v. Page, 7 How., 819, 829. 'This is necessary to enable the defendant to meet the fraud and the time of its discovery.' Moore v. Greene et al., 19 id. 69, 72. The same rules are laid down in Baubien v. Baubien, 23 id. 190, and in Badger v. Badger, 2 Wall., 95."

This Court then goes on to give many examples illustrating the rule thus emphatically announced, of which the following passage contains a few (141):

> "In Cole v. McGlathry (9 Mc. 131), the plaintiff had given the defendant money to pay certain

debts. The defendant falsely affirmed he had paid them, and fraudulently kept the money. It was held that the plaintiff could not recover, because he had at all times the means of discovering the truth by making inquiry of those who should have received the money.

"In McKown v. Whitmore (31 id. 448), the plaintiff handed the defendant money to be deposited for the plaintiff in bank. The defendant told the plaintiff that he had made the deposit. It was held that, if the statement were false and fraudulent, the plaintiff could not recover, because he might at all times have inquired of the bank. In Rouse v. Southard (39 id. 404), the defendant was sued as part owner of a vessel, for repairs, and pleaded the Statute of Limitations. The plaintiff offered evidence that the defendant, when called on for payment, had denied that he was such owner. It was held that, as the ownership might have been ascertained from other sources, the denial was not such a fraudulent concealment as would take the case out of the bar of the Statute.

"Numerous other cases to the same effect might be cited. They all show the light in which courts regard the qualification here in question, of the limitation which would otherwise apply."

See, also, *Consolidated Co. v. Scarborough,* 216 Cal. 698; *Lady Washington Co. v. Wood,* 113 Cal. 482; *Sacramento Lands Co. v. Lindquist* (C.C.A. 9), 39 Fed. (2d) 900; *Bradbury v. Higginson,* 167 Cal. 553.

In the face of this admitted rule, the court below accepted evidence (adduced by Petitioner) showing

what certain officers knew at the very time of the alleged fraud, as being proof that during the many years that followed, the Bank discovered no facts, and was not put on knowledge of any facts, charging it with notice of the allegedly fraudulent transaction.

Plaintiffs in the present case introduced no evidence whatever on the question of when the Bank learned the facts from which the inference of fraud was drawn. Petitioner, however, although not bound to, came forward with evidence to show that at the very time of the alleged fraud, in 1919, many officers and employees of the Bank knew the facts now put forward as constituting the alleged fraud, which facts, indeed, were common knowledge in the Bank at the time, as shown below.

The Trial Court Entirely Misconceived the Question of Laches and the Statute of Limitations.

The trial court, in its opinion, had this to say on the question of Laches and the Statute of Limitations:

> "Admittedly some of the bank officials knew that Herbert Fleishhacker was interested in a deal with the Bardes. * * *
>
> "In this connection it may be observed that while the officers of the Anglo knew of the transaction, it was not at that time known to plaintiff stockholders. * * *
>
> "The evidence shows that discovery [by plaintiff stockholders] of the facts upon which the charges of fraud are based was made in 1933. The

suit was filed on December 5, 1934, within the statutory period. The claim of laches is without merit." (R 190-191, 196)

In its finding the trial court found as follows:

"XIX. It is not true that the plaintiffs or their ancestors or predecessors in interest have been guilty of laches. It is not true that so long a time has elapsed since the matters and things complained of took place that it would be inequitable for this Court to take cognizance thereof.

"XX. It is not true that more than three years before the commencement of this action plaintiffs had knowledge or means of knowledge of the alleged fraudulent acts complained of in the Bill of Complaint, and it is not true that this action is barred by any provisions of the statute of limitations." (R 316)

* * * * * * *

"XI. The facts as to said profits were not known to stockholders of the bank, and none of the plaintiffs herein had any notice or knowledge whatever of the receiving by said Fleishhacker of such profits from the use of funds of the bank as hereinbefore alleged until about the year 1933. Plaintiffs discovered the facts hereinbefore alleged in the following manner:" (R 308)

This finding then continues with a long passage from the complaint, setting out the circumstances of discovery by plaintiff stockholders, in 1933, of the alleged fraud committed in 1919. (R 308-310)

The foregoing quotations from the trial court's opinion and findings demonstrate, we submit, that the trial court held that the Bank had knowledge of the alleged fraud at the time of its commission and (mistakenly believing, as did the plaintiffs, that the plaintiff stockholders and not the bank were the "aggrieved parties") erred in failing to find as requested by Petitioner; that because of the Bank's knowledge, the suit was barred by laches and the Statute of Limitations. (R 259, Nos. XV, XVI)

Treatment in the Court Below of Laches and the Statute of Limitations.

The court below attempted to make the trial court's error of law unimportant, by making a contradictory finding. It discussed Petitioner's evidence showing the extent of the knowledge of certain officers of the Bank at the time of the transaction itself, in 1919, and solely upon the basis of that evidence, concluded as a fact that the plaintiffs had sustained the burden of proving that no officers or responsible employees of the Bank knew, or discovered, or suspected, the facts of the alleged fraud at any time during the following fifteen years.

The foregoing appears plainly on the face of the opinion of the court below. (R 912-914)

If the facts from which the alleged fraud was inferred were discovered or suspected by any responsible bank officer at any time within the twelve-year period intervening between the alleged commission

thereof and December 5, 1931, then this action is barred by laches, by analogy to the three-year statute, this action having been brought December 5, 1934. The evidence that the Bank did not discover, or have reason to suspect, the facts from which the alleged fraud was inferred, at any time during these twelve years, consists exclusively of evidence concerning the knowledge thereof possessed by certain responsible officers of the Bank at the time of the transaction itself, in 1919. Basing its decision on that evidence alone, the court below concluded:

> "We are satisfied that the proof is such as to require a finding that the Bank did not discover the fraud until appellees brought it to light by their investigations. Hence the action is not barred as to the Bank. (R 912) * * *
>
> "It is true that the burden of proving lack of discovery by the Bank rested upon appellees. Earl v. Lofquist, supra; Lady Washington, etc., Co. v. Wood, supra; Consol. Reservoir & P. Co. v. Scarborough, supra. But we think this burden has been discharged." (R 914)

The court below did not mention the defense of laches (which was urged by Petitioner), but addressed itself only to the Statute of Limitations.

In the State Courts, This Action Would Be Governed by the Statute of Limitations.

Sec. 338, subd. 4 of the *California Code of Civil Procedure* provides: [Actions that must be brought within three years]:

> "4. An action for relief on the ground of fraud or mistake. The cause of action in such case not to be deemed to have accrued until the discovery, by the aggrieved party, of the facts constituting the fraud or mistake."

In California, all actions, whether legal or equitable, are governed by one or another of the provisions of the Statute of Limitations: *Piller v. Southern Pacific R. R. Co.,* 52 Cal. 42, 44.

And in California, as elsewhere, a suit in equity may be barred by laches, though brought within the period of the applicable statute: *Boone v. Templeman,* 158 Cal. 290, 299.

It is settled in California that stockholders' suits brought on behalf of the corporation, alleging fraud on the part of an officer or director, are governed by the statute above quoted: *Whitten v. Dabney* (1915) 171 Cal. 621, 628-629; *Pourroy v. Gardner* (1932) 122 Cal. App. 521, 531.

As the court said, in *Earl v. Lofquist* (1933) 135 Cal. App. 373, 376:

> "If the right to maintain the action is barred as to the corporation by the statute of limitations, neither the corporation nor a stockholder in its behalf, irrespective of when he became such, can maintain it. The fact that a stockholder is the nominal plaintiff does not in any manner enlarge the rights and remedies of the action (*Turner v. Markham,* 155 Cal. 562)."

Federal Courts in Equity Cases Follow State Statutes of Limitations by Analogy, Absent Special Circumstances.

This Court has recently summed up the effect in federal courts, sitting in equity, of state Statutes of Limitations: *Russell v. Todd,* ..... U. S. ....., 84 L. Ed. (Adv. Op.) 517, 60 S. Ct. 527. As was pointed out in that case, the federal courts, sitting in equity, are not governed by state Statutes of Limitations; but where (as here) the suit is one which, if brought in the state courts, would be governed by a state Statute of Limitations, then the federal courts, in determining whether the suit is barred by laches, will, when consonant with equitable principles, adopt and apply by analogy, the local Statutes of Limitations.

It follows that the present suit is barred by laches, quite apart from the prejudice (discussed below) which Petitioner has suffered because of the long delay. This because the period of the state Statute of Limitations applicable to such suits had not only run, but had run five times over.

And there being no evidence of any kind to excuse the delay by showing the Bank's ignorance of the facts (or that the Bank was dominated by Petitioner at any time during the fifteen-year period), the action necessarily fails. As shown below, moreover, it affirmatively appears, as was found by the trial court, that the facts were known to the Bank in 1919.

The Statute of Limitations Is in Issue.

Although the court below passed upon the issue of the Statute of Limitations, it remarked a doubt whether Petitioner was in a position to urge the bar of the Statute as having run against the Bank, stating that "The pleadings do not specifically frame an issue in respect of the Bank's notice or knowledge of the fraud." (R 912)

Except for this expression by the court below, there has been no intimation, either by counsel or by the trial court, questioning the fact that the Statute of Limitations was in issue; and the Statute has been treated as an issue throughout, both by court and counsel. Since the question is raised by the opinion of the court below, however, we deem it appropriate briefly to discuss the matter.

Perhaps the shortest answer to the suggestion of the court below that the Statute is not in issue, lies in the circumstance that state Statutes of Limitations, as such, are never a direct issue in a suit in equity in the federal courts: The action is barred by delay under the doctrine of laches; and the Statute of Limitations enters only as an analogy, the degree in which it will be regarded as controlling varying with the circumstances detailed in the opinion of this Court in *Russell v. Todd,* supra.

It is settled, therefore, that it is unnecessary to plead the Statute of Limitations in order to invoke laches as a defense. *Waller v. Texas & P. Ry. Co.,*

229 Fed. 87, 92, and cases cited; *Same case* (affirmed) 245 U. S. 398; *Stevenson v. Boyd,* 153 Cal. 630, 636.

As was stated in *Talmash v. Mugleston,* 4 L. J., Ch. (O.S.) 200-01:

> "The rule [of laches] * * * does not result from the statute of limitations. Suppose the rule to be adopted by analogy to the statute, that would not enable the defendant to plead the statute. * * *
>
> "But this Court, like every other, is bound to take notice of every public statute for the purposes of analogy, and of the statute of limitations among the rest. Where a court of equity proceeds by analogy to the statute, it is bound to know the statute, in order to apply the analogy. It is not necessary, therefore, to plead the statute; nor can the rule of the court, [that delay for the statutory period is laches], and the analogy on which it is founded, enable the party to protect himself by such a plea. * * * It can serve no end for him to put in a plea, which only states an act of parliament, to which the court, in applying its rules by analogy to that statute, would be bound to advert."

It is not disputed that laches was properly pleaded. (R 37, 73) We may observe in passing that laches would be in issue even if it had not been pleaded: *Hays v. Seattle,* 251 U. S. 233, 238; *Sullivan v. Portland, etc. R. R. Co.,* 94 U. S. 806, 811; *Richards v. Mackall,* 124 U. S. 183; *Akley v. Bassett,* 189 Cal. 625, 648.

There is no question but what this suit for an accounting of secret profits alleged to have been re-

ceived by an officer of the Bank, is one in equity: 3 Pomeroy, *Equity Jurisprudence* (4th Ed.) Secs. 1090, 1094; *Alexander v. Hillman,* 296 U. S. 222, 239; *Davis v. Pearce,* 30 F. (2d) 85, 88, and cases cited; *Farmers & Merchants' Bank v. Downey,* 53 Cal. 466, 468.

Quite apart from the foregoing, however, the Statute of Limitations, as such, was without doubt an issue in the case. The complaint showed on its face that the alleged cause of action arose fifteen years before the suit was brought. Plaintiffs (failing to realize that the Bank was the aggrieved party) did not allege any excuse for the Bank's delay. Petitioner pleaded the State of Limitations, both in the answer and by motion to dismiss (R 37, 73, 74); and the form of the plea was not questioned by plaintiffs, and in any event was adequate (Rules of Civil Procedure, Form 20, Fourth Defense).

Further references to the Record showing that the Statute was in issue could be multiplied, but we submit, without more, (a) that quite apart from the prejudice suffered by Petitioner because of fifteen years' delay, this suit is barred by laches, by analogy to the Statute of Limitations; and (b) as we presently show, Petitioner has suffered great prejudice from the long delay, and the action is barred for that reason, quite apart from the Statute of Limitations.

The Evidence Shows, the Plaintiffs Admitted, and the Trial Court Found, that the Bank had Notice in 1919.

We have shown that since it was the burden of plaintiffs to allege and prove that failure to sue for fifteen years was not laches because either the Bank did not have knowledge of the alleged fraud or was under Petitioner's domination, it was error of the trial court to fail to find, as requested, that the action was barred, there being no evidence concerning what the Bank knew or discovered between 1919 and 1934, and no evidence of domination.

We now show that the trial court did in fact find that the Bank had notice, in 1919, of the facts from which the court inferred fraud; and that the evidence establishes such notice.

The trial court, in its opinion, stated that,

> "Admittedly some of the Bank officials knew that Herbert Fleishhacker was interested in a deal with the Bardes." (R 190)

and that

> "In this connection it may be observed that while the officers of the Anglo knew of the transaction, it was not at the time known to plaintiff stockholders." (R 191)

This constituted notice to the Bank (*Curtis v. Connly,* 257 U. S. 260, 264). The statement of the trial court that "While the officers of the Anglo knew of the transaction, it was not at the time known to the

plaintiff stockholders" (R 191), is to say (we submit) that if the things that the court finds were known to the Bank officers, were known to the plaintiffs, the latter would be charged with notice.

As noted, the court below held on appeal, (a) that Petitioner's evidence of what was known to the Bank at the time of the transaction in 1919 was not sufficient to show that the Bank then had notice of the alleged fraud, and (b) that this evidence alone was sufficient to sustain plaintiffs' admitted burden of proving that the Bank did not know, or discover, or have grounds to suspect, or have means of ascertaining, the facts from which the alleged fraud was inferred, at any time during the following fifteen years.

As its ground for holding that the Bank was not then (in 1919) charged with notice, the court below said:

> " * * * at most the Bank knew the loans were to be used in a venture in which Fleishhacker was a partner. Burges * * * had been told by Alexander * * * that Fleishhacker was a partner in the steel venture; and nobody considered the matter a secret. But Burges believed, erroneously, that Fleishhacker was a partner in M. Barde & Sons, Inc.; he did not know the details." (R 913)
>
> Mortimer Fleishhacker "knew that the loans were to be used in the new enterprise, but he did not know that they were to be sent East as a deposit on the contract." (R 913) "But he thought that Herbert Fleishhacker 'was to personally put up a large sum of money and the Bardes were to match that sum'; that Herbert Fleishhacker and

the Bardes were to be partners 'and each in a substantial amount' ". (R 913)

"Herbert Fleishhacker stated that he discussed the loans with the * * * Finance Committee * * * explaining that the loans were to be made in connection with a steel deal in which he was to become a partner. It is significant, however, that Fleishhacker did not testify that he ever disclosed the particular terms of his deal with the Bardes. And, if the knowledge of Mortimer Fleishhacker is any criterion (and we think it unlikely that his colleagues on the Finance Committee[1] knew any more than he), it appears that the Bank was actually misled by Herbert Fleishhacker into believing that he, personally, was furnishing half the money for the venture." (R 913-14)

In essence this is to say that the Bank, its Finance Committee, and some of its officers, knew at the time that Petitioner was a partner with the Bardes in a steel venture, that the proceeds of the loans were to be used in that venture, and that no one considered the matter a secret; but that the Bank is not to be charged with notice, because: (a) one of the officers did not know the details and believed Petitioner was a partner in M. Barde & Sons, Inc.; (b) Mortimer Fleishhacker, while he knew the funds were to be used in the new enterprise, did not know they were to be sent East as a deposit on the contract; (c) Petitioner did not disclose the "particular terms" of his deal with the Bardes; and (d) since Mortimer Fleishhacker be-

(1) The two members who died prior to this suit. (R 914)

lieved Petitioner was supplying half the funds (which he was and did), and it was "unlikely" that the other members of the Finance Committee knew any more than he, "it appears that the Bank was actually misled into believing that he, personally, was furnishing half the money for the venture".

The evidence shows that Petitioner in fact did furnish one-half of the capital of the venture, and that the Bank and its officers had knowledge at the time (1919-1920) of the following:

1. That Petitioner was personally interested as a partner in the venture in which the proceeds of the loans were to be used. This was known not only to the members of the Finance Committee, but to other officers, and was a matter of common gossip in the Bank. (R 190, 313, 429, 604-05, 611-12, 624-25, 629, 679-81, 700)

2. That the members of the Executive Committee knew that Petitioner recommended the loans, because his recommendation was made to them. (R 651, 700)

3. That the Bank loans were paid with funds of the Steel Corporation. This was disclosed by the fact that three of the checks of the Steel Corporation in payment, drawn on the Bank, were made out to Petitioner, endorsed by him, delivered by him to the note desk, were cashed and the proceeds applied on the loans. Each check showed on its voucher portion and on its face that one-half the amount thereof was being charged by the corporation to Petitioner personally. (R 388, 614)

4. That Petitioner was a partner with the Bardes and the nature of the partnership. This is shown by a letterhead to that effect taken from the Bank's files at the time of the trial. The letter is dated January 28, 1921, and was written to the Bank. The letterhead lists the partners as follows (R 428):

> "Partners
> J. N. Barde
> H. Fleishhacker
> L. B. Barde
> H. Barde."

It contains the statement in bold printing that Barde Industrial Company was

> "Affiliated with Barde Steel Products Corporation New York City selling 500,000 Tons Steel of U. S. Shipping Board and U. S. Navy";

and that

> "This Company was formed to handle the surplus steel and equipment accumulated by the Government and various industrial corporations throughout the country through cancellation of the war time contracts." (R 429)

5. That Petitioner's stock in the Steel Corporation was issued in the names of nominees, for one of these was an officer and the other an employee of the Bank, one of whom, Klinker, was instructed to include the dividends thereon in Petitioner's income tax return. (R 466)

6. That salary was paid to Petitioner by the Steel Corporation, because the check in payment of the

$50,000 salary was drawn on the Bank, payable to the order of Petitioner, was endorsed by him, and cashed through the Bank. (R 386)

7. The Bank itself was a beneficiary under the agreement dated March 22, 1922, by which the partnership was dissolved, and it must be presumed that it had notice thereof because under such agreement the Bank received certain mortgages. (R 20, 23-24)

8. The Bank therefore knew not only that Petitioner was in the venture in order to receive returns therefrom; it also had ready means of knowing that he received salary and dividends, and an agreed price when he sold out his interest to the Bardes.

9. The facts regarding the Bardes' $175,000 loan at the Central Bank, including Petitioner's guaranty, are shown by the Bank records. On December 22, 1919, the Anglo Bank wrote the Central Bank advising it that on Petitioner's instructions it was debiting the Central National Bank with $175,000, and enclosing the note of M. Barde & Sons for that amount. (R 640, 683) The Bank files contain the letter of the Central National Bank, dated December 23, 1919, acknowledging receipt of the Barde note "together with the guaranty of Herbert Fleishhacker in like amount". The Bank records therefore showed at the time, all of the particulars of the Barde loan at the Central National Bank and Petitioner's guaranty thereof.

10. While the Court below states in its opinion that Mortimer Fleishhacker did not know that any

part of the proceeds of the loans were to be sent East as a deposit on the contract, the Bank records contained a letter of M. Barde & Sons, dated December 16, 1919, carrying a pencil notation by some bank officer that the $250,000 loan proceeds were credited to the Guaranty Trust Company New York. (R 638)

11. The Bank in fact forwarded the $250,000 loan proceeds to Guaranty Trust Company in New York for the account of L. B. Barde. As the Record shows, the same was credited to his account in that Bank on December 23, 1919. (R 532) The Record also shows the Bank knew the disposition of the $325,000 of Anglo Bank loans and the $175,000 Central Bank loans because Klinker, an officer of the Bank, handled the details as to what was done with that $500,000. (R 703)

12. Besides the knowledge which the Bank had of the agreement of dissolution dated March 22, 1922, and that Petitioner sold his interests in the venture to the Bardes and received $200,000 therefor (because it was a beneficiary under that agreement), the Bank also knew all the facts leading up to the making of that agreement and sale, because Klinker, an officer of the Bank, handled the details of the investigation which disclosed the Bardes' abstraction of $200,000 of assets which was the identical amount subsequently received by Petitioner under the agreement of dissolution. (R 690) In fact, Klinker was the person who discovered J. N. Barde's irregularities which led up to the investigation made by him and the subsequent agreement of dissolution. (R 426)

The court below does not know any facts that were not known to the Bank in 1919; yet it has found that a selection from among these same facts are sufficient to sustain an inference that Petitioner committed a fraud and a crime. If they were sufficient for that purpose, were they not much more than sufficient to have put the Bank on inquiry?

The trial court found that there was no express agreement, as alleged, but that there was (in some confused sense) an implied agreement. The court below agreed that there was no express agreement, and "no direct proof" of any agreement, but found by inference that there was an implied agreement, basing its finding to this effect on a view of the facts both different from and contradictory of the view of the facts taken by the trial court.

The point we now make is that in both courts, the finding of a fraudulent agreement rested on acts, not on words, and those acts were known to the Bank and its officers at the time of the transaction.

To say that the Bank's knowledge of the facts did not put it on notice of the inferences which the court below draws therefrom is to say that there is no such thing as a corporation's being put on notice of a fraud, unless some explicit notation of the actual fraud appears in the books and records of the corporation or there is a confession. The application of any such rule would wipe out the protection accorded by the statute of limitations and the doctrine of laches, doctrines which have long been held to be "vital to the

welfare of society and are favored in the law * * * [and] found and approved in all systems of enlightened jurisprudence." (*Wood v. Carpenter,* 101 U. S. 135, 139)

From all the foregoing we submit that if the burden of proof had been upon Petitioner (which it was not) to show affirmatively that the Bank was put upon notice of the alleged fraud fifteen years before the suit was filed, that burden would have been abundantly discharged.

It follows that the suit should have been dismissed on the ground of the laches of the Bank.

Petitioner has Suffered Inequitable Prejudice, and the Suit is Barred by Laches.

Independently of the analogy of the Statute of Limitations, the delay in bringing this suit, in connection with intervening facts and circumstances, has resulted in prejudice to the defendants of such inequitable nature that it is barred by laches. Among the intervening prejudicial facts and circumstances are:

1. The delay of approximately fifteen years between the transactions complained of in December 1919 and the commencement of this suit in December 1934. (R 7, 32)

2. The delay of approximately seventeen years eight months between the transactions complained of and the trial of this suit in August 1937. (R 353)

3. The intervening death of L. B. Barde (R 362), with whom Petitioner made the partnership agreement, thus making it impossible to obtain the testimony of the one person who would have been in a position to corroborate Petitioner's own testimony concerning that agreement.

4. The intervening deaths of Sigmund Stern and J. J. Mack (R 599, 617), who were members of the Bank's Finance Committee at the time of the loans (R 599), and to whom Petitioner disclosed his interest in the venture for which the loans were made (R 678, 679, 700), and who passed on and approved the loans. (R 599, 601, 618)

5. The intervening death of E. R. Alexander (R 611, 617), who was Assistant Vice-President (R 680), Assistant Cashier (R 683, 684), the Executive Officer (R 617) in charge of the Note Department (R 612), and one of the officers who attended Finance Committee meetings. (R 600, 604) Petitioner had disclosed his interest in the venture to Mr. Alexander (R 701), and the latter had discussed the same with Ernest J. Burges. (R 604, 611, 612) In addition, Alexander forwarded the Barde $175,000 note to the Central National Bank of Oakland. (R 683, 684) Mr. Alexander could have given invaluable testimony as to what occurred in the Bank when it made the loans.

6. The intervening death (R 680) of W. E. Wilcox, Vice-President and Cashier. (R 447) Mr. Wilcox, on behalf of the Bank, was connected with certain details of the loans (R 680, 700), and, if living, might

have been able to give definite testimony concerning the same.

7. The intervening deaths of thirteen of the nineteen Directors of the Bank at the time of the loans. (R 599)

8. The removal of the offices of the Bank on two occasions since the transactions in question (R 650), and the possible loss or misplacing of records or correspondence that might have been of value in the defense of this suit.

9. The impossibility, due to lapse of time, of certain and detailed recollection of various facts by several of the witnesses, viz: Samuel Hauser (R 420-4); Etienne Lang (R 547); Mortimer Fleishhacker (R 618-50); and Petitioner.[1] (R 654-703)

Lapse of time in the prosecution of a cause of action which, with intervening circumstances, results in prejudice in the defense of a suit, constitutes laches and operates to bar the action, and such defense, with prejudice shown, may be upheld even though the statutory period of limitation has not elapsed.

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(1) In connection with the question of Petitioner's veracity, it should be noted that in almost every instance when he admitted his lack of definite recollection he could, if he had had any disposition to be untruthful, have given positive and favorable testimony in his own behalf, without contradiction in the record. A dishonest person is seldom without the necessary recollection to fully exculpate himself on all important matters of fact, and even as to minor and immaterial details, and seldom overlooks an opportunity of so doing. Such a person's recollection is usually found to be dim only as to matters of fact that are unfavorable to his cause.

Lapse of time for such a period that it may be reasonably supposed that prejudice has resulted, casts the burden on the plaintiff to show the absence of prejudice. (*Cahill v. Superior Court* (1904) 145 Cal. 42, 47; *Hammond v. Hopkins,* 143 U. S. 224; *Abraham v. Ordway,* 158 U. S. 416, 421)

When, as in the case at bar, there has been great prejudice, and the statutory period of limitation has not only run but has run five times over, a clear case is presented for the application of the doctrine of laches.

In addition to the elements of prejudice already summarized, Petitioner has been greatly prejudiced by the delay, because a claim for interest was allowed which exceeds the amount of the alleged profits. The amount of the judgment is $736,485.57. Of this $348,-125.00 represents the amount of the alleged profits. The remainder, $388,360.57, represents interest thereon. The accumulation of this amount of the interest, because of the long delay in bringing suit, is obviously an element of prejudice. See *Waller v. Texas & Pac. Ry. Co.,* 245 U. S. 398, 412.

POINT III.

THE COURT BELOW HAS SO FAR DEPARTED FROM THE ACCEPTED COURSE OF JUDICIAL PROCEEDINGS AND HAS SO FAR SANCTIONED SUCH DEPARTURES BY THE TRIAL COURT, AS TO CALL FOR EXERCISE OF THIS COURT'S POWER OF SUPERVISION.

The Findings were Prepared by Counsel and Signed Without Change. They are Inconsistent with the Trial Court's Opinion on vital Points and Not Supported by Evidence.

In the present case, the trial judge not only permitted the successful party to prepare the findings, but signed them without any change (R 766); and this notwithstanding that the findings (directed to conform with the opinion (R 197)) change, contradict and are otherwise inconsistent with the view of the facts expressed in the judge's opinion.

Petitioner submitted a detailed request for findings, exceptions to and suggested modifications of plaintiff's proposed findings, and two requests for an opportunity to be heard in connection with settlement of the findings. (R 763-4) All of these were denied (R 765), and plaintiffs' proposed findings were signed as drawn, without any hearing. (R 765-6)

Occasional judicial pronouncements emphasize (what is obvious in any event) that the practice of permitting counsel to prepare the findings of fact and conclusions of law, unless carefully guarded, is dangerous.

In *Process Engineers v. Container Corporation,* 70 F. (2d) 487, 489, the court said:

> "It is urged that the court's findings should be sustained because supported by some evidence. The weakness of this argument lies in the fact that the findings were not made by the court, but are the work of industrious counsel who combined his argument and a partisan and unfair statement of facts into one and called it, 'Findings of Fact.' * * *
>
> "Such so-called findings do not help an appellate court. They reflect the views of counsel who submitted them and detract from the force and effect which are ordinarily given to findings made by the trial judge. When the abuse is aggravated (and the objectionable practice is growing), the assistance to the appellate court, which findings when carefully made by the trial court afford, is lost, and it becomes necessary for us to study the evidence as though no findings had been made by the District Court."

The court, in *Brenger v. Brenger,* 142 Wis. 26 (125 N. W. 109, 113), stated:

> "We are rather forced to the conclusion that the finding belongs to a class, often found troublesome and sometimes fatal to a judgment; those made by judicial sanction of a draft prepared by attorneys for the prevailing party, following some general suggestions from the bench as to the disposition of the case that would be made. That is a very dangerous practice, in the judgment of the writer; a practice which fails to respond to the command of the statute that 'the

judge shall state in his decision separately: (1) The facts found by him: and (2) his conclusions of law thereon.' As said, in effect, on another occasion, 'Such practice, in the judgment of the writer, unless very closely guarded, might well be discontinued altogether.'

"'Experience shows that counsel, the most able, honorable and conscientious, * * * after the close of a hotly contested case, are not in the frame of mind, ordinarily, best suited to draft the findings which must express the judgment of the court. That is no criticism. It is only an acknowledgment of the natural infirmities of the most perfect of us. All are affected, regardless of ability or purity; the difference is in degree. The making of the findings is purely a judicial function.' Harrigan v. Gilchrist, 121 Wis. 127, 396, 99 N. W. 909.

"Except so far as sanctioned by custom, I know of no warrant for judicial findings to be made up of suggestions as to form and substance, by prevailing counsel, with or without general declarations from the judicial head as to conclusions. The calm sea level, so to speak, of the judicial view is required to respond to the spirit of the Code. It should be seen that these observations are on the writer's personal responsibility, but they are the result of surveys from the viewpoints of a practitioner, a circuit judge and a member of this Court. Doubtless where a judge scans proposed findings eliminating everything not properly a part of such a determination as the statute contemplates, and seeing that all matters of material fact are covered, the preparation of

the paper by counsel proves helpful and is without objection. A practice in that respect so guarded would greatly aid in the administration of justice and is, perhaps, necessary, especially in case of a heavy burden of judicial work.

"If what has already been said does not fully justify the criticisms made of the manner the findings were prepared, the following in connection therewith probably will:"

And in *Nashville, C. & St. L. Ry. Co. v. Price,* 125 Tenn. 646, the court said:

" * * * In accordance with this demand of the trial judge, there was a written findings of fact prepared by the attorney for plaintiffs below. It was signed by the judge and is put into the record as his finding.

"This practice is improper. * * * Such findings are accorded the highest dignity in the appellate courts of Tennessee. They are looked to as embodying a fair statement of all the essential facts in the record, and this Court has said, in Hinton v. Insurance Co., 110 Tenn. 130, 72 S. W. 118, that it will not go outside this finding and examine the record at large for the facts of the case, but will only look to the record to see if the findings of fact are supported by any evidence. There are other cases, familiar to the profession, which further illustrate the weight and force that are here given to these findings of the trial judge.

"The preparation of such a finding, being a matter of so much importance and a high judicial function, cannot properly be intrusted to counsel. Counsel have a natural bias with respect to cases

in which they are engaged that makes it well-nigh impossible for them to fairly and fully present all the facts as the judge would do. We are of opinion, therefore, that his honor was in error in delegating the preparation of the duty imposed upon him by the statute to counsel in the case, and that the finding in this record cannot be looked to by us and treated as a statutory finding of facts by the trial judge. Had exception been taken, the case would have been reversed on this account.

"However, no error being assigned to this action of the trial judge, we have examined the record, as if no special finding had been requested, to see if there is evidence to sustain the judgment below."

It is said in 12 Jour. Am. Jud. Soc., p. 185:

"* * * The *weakest* link in our chain of administering justice is the failure to find the facts as they exist. *Where there is such failure the wrong can never be righted.*" (Emphasis in original)

The following quotation is from an address by Mr. Justice Morgan of the Supreme Court of Idaho:

"* * * it is the practice * * * that the attorney for the party litigant who has won his suit is called upon to prepare the findings for the signature of the trial Judge. * * * Now, you could not find a more biased and prejudiced and badly warped source than that. * * * I have no objection to a trial Judge assigning the duty of preparing the findings to the attorney who wins the case.

> But, I would like to have the trial Judge certify that that is what occurred, rather than to leave it to the speculation of the Supreme Court as to whether the trial Judge prepared those findings or not. * * * if the attorney for the respondent makes those findings, and the Trial Judge merely supplies the signature, it ought not to be binding upon the appellate court, because it does not arise from an unbiased source." (Proceedings, Idaho State Bar, 1937, p. 95.)

In the present case, even the form of the findings is strikingly improper. Much of the material in them is simply copied from the complaint, including at several points the words "hereinbefore alleged" or similar expressions. (e.g., R 308, 310)

We now show in parallel columns a few of the many inconsistencies between the trial court's view of the facts as expressed in its opinion, and the view of the facts embodied in the findings drawn by counsel and signed by the court.

The Opinion	*The Findings*
"Herbert Fleishhacker was the president and chief executive officer of the Anglo Bank, receiving an annual salary of $50,000." (R 176)	Herbert Fleishhacker "was president of the bank and chief executive officer thereof in active control of the management of the bank and its operations, and * * * was paid a salary * * * to devote his time and attention to the affairs of the bank, * * *" (R 296)

While this finding appears at first glance to be innocuous, it suggests by implication, (1) that the management of the Bank was under Petitioner's con-

trol and domination, and (2) that under his terms of employment he was not permitted to engage in other activities but was required to devote all of his time and attention to the Bank, both of which implications are contrary to the facts and to the evidence.[1]

The Opinion	*The Findings*
(No such findng).	" * * * said Fleishhacker caused the defendant bank, * * * to loan and advance the sum of $250,000 * * * and caused the defendant bank to advance the further sum of $75,000," (R 298-9)

In its opinion, the court did not find that Petitioner caused the Bank to make the loans in question. All it found was that he "recommended" the loans. (R 178, 189, 190) The finding that Petitioner caused the loans to be made implies either that he was the sole actor for the Bank in the matter, or that the other Bank officers who acted were his puppets.

There is no evidence to sustain a finding that Petitioner "caused" the loans to be made, it being clear that he did not; and the trial court's opinion shows plainly that the judge did not believe any such thing.

The Opinion	*The Findings*
"No showing was made that the loans were ever approved by the board of directors" (R 180)	The "loans * * * were not approved by the board of directors of said bank." (R 300)

(1) There is no implied condition that a bank officer must devote all his time to bank affairs. A corporation officer may engage in outside activities, so long as he acts in good faith. (64 A. L. R. 784)

There is no evidence that these loans were not approved by the Board of Directors.

What the evidence showed was that the Finance Committee had full authority to make loans, and that it made and approved these loans (R 678, 204) The trial court, on the hearing of defendants' motion for leave to introduce in evidence the By-Law of the Bank which shows that the Finance Committee had complete authority in the matter, and also that the Board of Directors in fact approved the loans, said that its statement in the Opinion that no showing had been made that the loans were ever approved by the Board of Directors, constituted purely an incidental remark. (R 751, 752)

The finding in question carries the implication of an irregularity that never occurred, and which the trial court knew never occurred.

The Opinion

"Approximately $1,000,000 would be needed 'to launch the enterprise.' A bidder required $250,000 to qualify his bid. Of the $1,000,000 needed, the sum of $400,000 (including the $250,000 for qualification) would have to be deposited * * * as a guaranty fund, and in addition $500,000 in cash or surety bond for faithful performance. The remaining $100,000 would be for operating capital * * *" (R 176)

The Findings

"* * * defendant Fleishhacker was advised * * * and knew that $250,000 in cash was required to launch the enterprise, * * * [and] that an additional $250,000 would be required * * *" (R 298)

"Said loans and advances aggregating $500,000 constituted the amount of money required to finance the said venture * * *" (R 299)

There is no statement in the findings, as there is in the court's opinion, that the total capital required was $1,000,000, which included the $500,000 supplied by Petitioner. The statement in the findings that only $500,000 was required in the venture, is incorrect, as the opinion and the evidence show.

The Opinion	*The Findings*
(No such finding).	Herbert Fleishhacker "agreed and undertook to finance the said venture, and thereupon * * * caused the defendant bank * * * to loan [the money]. * * * said loans * * * constituted the amount * * * which defendant Fleishhacker had undertaken to procure and make available for the purpose of financing said venture in which he * * * was to have a one-half interest * * *" (R 298-300)

The findings are designed to import a precedent agreement and undertaking by Petitioner, no suggestion of which appears in the court's opinion, or in the evidence. On the contrary, as shown above, the trial court believed, as the evidence showed, that the partnership was formed before Petitioner learned that the Bardes desired to borrow, whether from the Bank or elsewhere.

The Opinion

"* * * upon the recommendation of Fleishhacker, the Anglo Bank loaned the money which made the venture possible. * * * The business was profitable, Fleishhacker's share thereof amounting to about $300,000. Under these circumstances may it not be said that Fleishhacker, president of a national bank, received a thing of value * * * for procuring from his bank a loan to launch the venture?" (R 189-90)

The Findings

"Part of the consideration for the said loans * * * was an agreement between said Bardes and said Fleishhacker that said Fleishhacker should participate in the profits of the enterprise" (R 300)

The reasoning of the trial court on this point is discussed at length below. It must suffice here to say that the trial court plainly believed it to be untrue that there was any factual understanding that Petitioner would receive an interest in the venture if the loans were obtained.

The Opinion

"* * * the Bardes delivered to the Anglo Bank as collateral security * * * Liberty Bonds of the value of $200,000 or more" (R 178); "The loans from the Anglo to [the Bardes] were fully protected." (R 186)

The Findings

The Bardes "delivered to the defendant Fleishhacker or the defendant Bank collateral security consisting of United States Liberty Bonds of the value of $200,000 or thereabouts." (R 300)

The findings import the suggestion that the securities may have been delivered to Petitioner personally; and omit the fact stated in the court's opinion, that the loans were fully protected.

The Opinion	*The Findings*
Barde Steel Products Corporation "subsequently [i. e., after 1919] borrowed on unsecured notes large sums from the Anglo Bank, aggregating at one time $118,000." (R 181)	"Fleishhacker during the year 1920-21-22 caused the defendant Bank * * * to loan other and additional large sums of money to said Barde Steel Products Corporation, such sums aggregating at one time as much as $118,000" (R 308)

There is no evidence whatever as to these loans, except that they were made. There was no evidence that Petitioner had anything to do with them, let alone that he caused them to be made.

The Court Below gave Full Effect to the Findings, Ignoring Discrepancies Between the Findings and the Opinion.

If the opinion of the court below is read in the light of the foregoing, it will be seen that (although the point was argued elaborately and at length) it gave full effect to the most exaggerated discrepancies between the view of the facts entertained by the trial court as expressed in its opinion, on the one hand, and counsel's findings of fact on the other. It will be seen, moreover, that the court below went further, and added to the findings by drawing additional inferences of its own therefrom wherever further findings were necessary to support the decision.

We submit:

(1) That the present case is an extreme example of an undesirable practice concerning the preparation of findings;[1]

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(1) See *Morgan v. United States,* 304 U. S. 1, 19-20.

(2) That such findings, if accepted on appeal, frustrate the appellate process;

(3) That in view of the new Rules of Civil Procedure,[1] findings of fact are now of much greater importance in the administration of justice in the federal courts than heretofore.

The Decision Below Violates Fundamental Principles of the Exigencies of Proof of Fraud.

It has been settled for a long time that fraud is never presumed; that where the evidence or the inferences which it will bear are ambiguous, the presumption favors fair dealing; and that when two inconsistent inferences may equally be drawn, that favoring honesty must be drawn. These principles are particularly important in cases where the charge of fraud is brought forward many years after the event, and after many witnesses have died and the memory of the survivors has been dimmed by time.

In this case it is admitted by both of the inferior courts that there was no express agreement that Petitioner should receive something in exchange for the loans made by the Bank to the Bardes. Everything depends upon inference from conduct. The court below sustains the charge of fraud by drawing inferences from acts which are at least equally consistent with entire honesty. (See Point IV, infra)

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(1) Equity Rule 70½ (now Rule 52(a) Federal Rules of Civil Procedure).

The following authorities are illustrative of the fundamental principle that charges of fraud, particularly stale charges of fraud, are to be examined with great care, and are required to be supported by clear and convincing proof.

Stearns v. Page, 7 How. 818, 829;
Halstead v. Grinnan, 152 U. S. 412, 416;
United States v. Arredondo, 6 Peters, 691, 716;
Fidelity & Deposit Co. v. Grand Nat. Bank (C. C. A., 8) 69 F. (2d) 177, 180-83.

The Opinion in the Court Below Recites the Facts That Appear Suspicious, and Fails to Mention Many Undisputed Facts Tending to Rebut the Charge of Fraud.

On the merits, the opinion of the court below might seem to indicate that the conclusion in favor of fraud is sufficiently supported by evidence to justify its being left undisturbed.

The fact is, however, that this impression is possible only because the opinion of the court below (a) accepts without question the partisan findings prepared by counsel, (b) draws further inferences therefrom when necessary, adds to and contradicts the trial court's view of the facts, and (c) fails to mention numerous undisputed facts and circumstances which show that taking the record as a whole, the evidence is entirely consistent with complete honesty.

We now set out a brief recital of facts, stated chronologically, each of which was either expressly

found to be true by the trial court or is shown by uncontradicted and unquestioned evidence.

We ask the court to contrast this recital with the highly selective statement of the facts in the opinion of the court below.

Facts not mentioned in the opinion of the court below are marked with asterisks.

The Facts.

L. B. Barde and J. N. Barde were brothers living in Portland, Oregon, doing business through their corporation under the name of M. Barde & Sons, Inc., with a net worth of $750,000.* (R 607) Their corporation had done business for a considerable period with the Bank;* and its financial condition was known to the latter's Finance Committee,* its loaning agency, which had authorized an unsecured credit line of $111,000.* (R 451)

L. B. Barde had married a cousin of Petitioner, had introduced himself, and on previous occasions had invited him to join in various ventures, all on a 50-50 basis.* (R 617, 622-3, 654, 655-63, 701-2, 704) For example, in one such proposal, made some months earlier, L. B. Barde wrote Petitioner, "We are prepared to invest One Hundred Thousand Dollars, and you to put in a similar amount."* (R 622)

Petitioner was a man of large means, and engaged in many business enterprises.* (R 621, 654-63, 701-4)

Some time before December 1919, L. B. Barde* proposed that Petitioner become a 50-50 partner with

*Not mentioned in the opinion of the court below.

them in a venture to buy steel from the Shipping Board and resell it. (R 176, 663) The amount of capital consisting of cash or credit was known to be $1,000,000.* (R 176, 364, 664-6, 666, 669, 702-4) The Bardes were to supply half in cash,* and Petitioner was to supply the remaining half in the form of cash, securities, or a bond as required by the Shipping Board* (R 177, 666, 669, 697, 702), and each was to receive a half interest. (R 176, 669, 704) This was agreed to between L. B. Barde and Petitioner, subject to an investigation as to whether the venture was a desirable one. (R 177, 663)

After independent investigation, the parties, about December 1, 1919, agreed to go forward in the venture. (R 177) L. B. Barde reported from the East that $500,000 in cash would be required,* and that the Shipping Board would accept an indemnity bond for $500,000 to secure performance of the contract.* (R 676) This was the half of the capital that Petitioner had agreed to supply as consideration for his half interest.* (R 666, 669, 702)

At this time, as the trial court found in its opinion, it had not been suggested that the Bardes would desire to borrow, whether from the Bank or elsewhere. (R 177, 665, 675) Petitioner testified that he believed the Bardes had the money.* (R 675, 696)

The Bardes thereafter (and only thereafter) asked Petitioner if they could borrow at the Bank. (R 177,

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*Not mentioned in the opinion of the court below.

298, 665, 670, 675, 696, 697) Petitioner presented to the Finance Committee, the loaning agency, Bardes' application for a loan of $250,000 and recommended that it be granted. (R 678, 679, 681, 700) A few days later, he received and presented their application for an additional $75,000. (R 697, 698) Both loans were granted by the Finance Committee. Petitioner did not participate in its action.* (R 599, 601, 618, 636-7, 640, 678-9) The Committee was advised by Petitioner and knew that the funds were to be used in this venture and that he had a personal interest and hoped to make a profit. (R 190, 313, 429, 604-05, 611-12, 620-1, 624-6, 629, 644-6, 652-3, 679, 681, 700) The loans were 6% demand notes of M. Barde and Sons, Inc. endorsed by J. N. Barde and secured by Liberty Bonds of the value of more than $200,000 (R 178, 300, 372-3, 375), and were "fully protected".* (R 186) They were handled in the regular course by the Committee,* which was familiar with the Bardes' credit standing* (R 599-606, 618, 620, 624-5, 629, 634-5, 636-7, 640, 644-5, 649-51, 675, 678-81, 700-1);[1] they were formally recorded* (R 600-6, 618, 636-7); there was no secrecy, and Petitioner's personal interest in the venture, and the fact that the proceeds were used in that venture, were common knowledge in the Bank.* (R 190, 313, 429, 604-5, 611-12, 620-1, 624-6, 629, 644-6, 652-3, 678-81, 700)

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*Not mentioned in the opinion of the court below.

(1) A financial statement dated as of December 23, 1919, of M. Barde & Sons, Inc. showing a net worth of $750,000 was found in the Bank's files. (R 180, 606-7, 639)

Petitioner was unwilling to present to the Bank, the Bardes' request for an additional loan of $175,000* (R 681), but arranged for a loan of this amount to them by the Central National Bank of Oakland, which he personally guaranteed. (R 682)

Of the borrowed money, $250,000 was used as earnest money on the bid to the Shipping Board. On the acceptance of the bid, the Steel Corporation was organized on January 6, 1920 "as an entity for carrying on the enterprise" to use the language of the court below. (R 902)

On January 8, 1920, Petitioner delivered his $500,000 indemnity bond to the Fidelity and Deposit Company of Maryland and thereby obtained its $500,000 bond guaranteeing performance by the Steel Corporation of the Shipping Board contract. (R 685, 687-8) This was done by him pursuant to the terms of the partnership agreement (R 702) as above set forth.* On the same day, the Steel Corporation, in consideration of the payment to it of the $500,000 in cash, and the accepted bid and the contract (of which the $500,000 bond supplied by Petitioner was an express and essential condition (R 86)) to be executed pursuant thereto, authorized the issue to L. B. Barde or his nominees, of 5000 shares of preferred stock and 10,000 shares of common. This stock was issued—one-half to the Bardes and one-half to Petitioner's nominees. In this manner the agreed respective contributions to capital were made and the agreed

*Not mentioned in the opinion of the court below.

respective participating interests were distributed.[1] The Shipping Board executed the contract, secured by $400,000 of the cash, and the $500,000 bond issued upon Petitioner's indemnity. The remaining $100,000 of cash was employed as working capital.

The Steel Corporation paid the Bank loans within four months. Half the amount so paid was charged on its books to the Bardes and half to Petitioner.*

The profits of the Steel Corporation were:*

1920—$ 95,253.28
1921— 140,946.14
1922— 141,807.94

Petitioner received from the Steel Corporation salary amounting to $75,000, and each of the Bardes a like amount, but payment of salaries was discontinued at Petitioner's request.* Petitioner was credited on the books of Barde Industrial Company (a unit of the enterprise) with a dividend of $73,123 on October 1, 1922, and sold his interest in the venture and related ventures to the Bardes for $200,000 on March 22, 1923.

In October 1932 an attorney, employed by one Lang to investigate certain claims against the Bank

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(1) The court below refers to the equal division of the stock, but without mentioning the fact that any other division would have violated the partners' first and only agreement, puts forth as significant, or suspicious, the fact that the stock was issued formally in exchange for the bid and the cash capital.

*Not mentioned in the opinion of the court below.

arising out of oil transactions, called his attention to an item in a detective's report showing that Petitioner had been a partner in the steel venture with the Bardes.* He advised investigating the matter because it might prove to be of assistance in the oil claims.* (R 459) The investigation was made. On October 29, 1934, Lang wrote demanding the Bank bring action against Petitioner. On November 13, 1934, the Bank adopted a resolution declining to bring action,* and this suit was filed December 5th.

In the fifteen years intervening between the date of the loans and the commencement of the suit, two of the four members of the Finance Committee died; E. R. Alexander, the Executive Officer in charge of the note desk, and who attended the Finance Committee meetings, died:* 13 of the 19 directors in office when the loans were made, died:* the Bank had moved its offices twice and records were missing:* and L. B. Barde, with whom Petitioner made the partnership agreement,* died before the trial.*

Interpretation of the Facts.

Having in mind the admitted law, that when these loans were made a national bank officer could personally borrow from the bank:* that at present national banks may lend to partnerships in which their officers own a 50% interest:* and to corporations in which officers own a majority interest:* that it is not a breach of trust for a corporate officer to recommend a transaction in which he is personally interested if

*Not mentioned in the opinion of the court below.

the transaction is fair to the corporation:* that Petitioner did not act for the Bank in making the loans,* but only recommended them to the Finance Committee, which independently without his participation,* and after investigation* and with knowledge communicated by him of his personal interest in the venture in which they were to be used, authorized them in behalf of the Bank: that they were handled in the regular course:* that there was no secrecy and Petitioner's personal interest in the venture was a matter of common knowledge:* that the loans were sound and desirable and secured by Liberty Bonds and evidenced by notes of a corporation that had previously dealt with the Bank and had been granted unsecured credit up to $111,000;* that the notes were indorsed and guaranteed by J. N. Barde; that the loans were promptly paid—having all these things in mind, it seems inconceivable that many years later a judgment of $736,485 ($852,729.21 as of June 30, 1940) should be rendered against a man whose affairs (by reason thereof) are now in the bankruptcy court, in favor of a Bank which made a good loan, repaid more than 15 years ago, and within four months of the time it was made.

Every single one of the facts we have recited above is established by the evidence; and more, they were admitted as true by plaintiffs and were found to be true in the trial court's opinion. If these facts were recited in the opinion of the court below, no one would

*Not mentioned in the opinion of the court below.

suggest that they presented a foundation for a judgment that a fraud and a crime had been committed. Can it be that the answer to questions of such importance should depend upon how the facts in an action are arranged and recited?

The trial court found that there was no express agreement for a bonus: it found that there was, in some obscure sense, an implied agreement, and it found the latter, by a process of inference. The court below admits that there is no direct proof to sustain that conclusion. Bearing this in mind, as well as the presumptions in favor of honesty and fair dealing, does not the mere circumstance that the facts can fairly be set down so as to permit, and indeed strongly support, the conclusion that no wrong was committed, compel a finding to that effect, for if an inference of fair dealing can be as readily drawn as an inference of wrongdoing or fraud, the inference of fair dealing must be drawn. And if the facts are such as only to permit the court to say that an inference of fraud "can be drawn", rather than "must be drawn", then the plaintiffs cannot prevail.

The Court below Recast the Whole Factual Setting; and its Decision Rests on a View of the Facts which Contradicts that of the Trial Court.

On the three main issues, the court below affirmed the judgment on the basis of its own inferential findings of fact, which either contradict the trial court's view, or add entirely new inferences to those drawn by the trial court.

Because of the trial court's errors of law, the court below had either to reverse the judgment, or to marshall the whole factual setting anew, and to make fundamental findings and inferences of fact contradictory of the view entertained by the trial court. It chose the latter course:

1. On the merits, the trial court took the position that although admittedly there was no express agreement that Petitioner should receive consideration for the loans or recommending them, there was (in some obscure sense) an implied agreement: the court seemed to believe that since Petitioner recommended the loans, knowing the proceeds were to be used in a venture in which he had an interest, and since that venture (and so, in some sense, the loans) resulted in large profits to Petitioner, it could be said that Petitioner received something of value for the loans or for recommending them. (R 189-90)

The court below took a wholly different view. It contradicted the trial court's finding that the partnership had been formed before the loans were mentioned, and found that the partnership was still only a tentative arrangement at the time the loans were sought. On this basis, it concluded that Petitioner, by continuing with the venture, could be said to have accepted his interest therein in exchange for the loans or for his recommendation of them.

It is indisputable that the trial court had no such idea at all, and indeed that this view is contradicted by the view of the facts entertained by the trial court.

2. Concerning Equity Rule 27 (Rules of Procedure 23(b)), the court supplied a finding, admittedly not made by the trial court, that the Directors of the Bank were guilty of bad faith in refusing to bring the suit; this upon grounds shown by the dissenting opinion to be insufficient.

3. Concerning laches and the Statute of Limitations, the trial court (failing to see that the cause of action was the Bank's and that the Bank was the aggrieved party), held that although "the officers of the Anglo knew of the transaction [at the time it occurred], it was not at that time known to plaintiff stockholders". (R 191) It held on this obviously erroneous ground that the knowledge of the Bank and the delay of fifteen years were irrelevant.

The court below met this difficulty by contradicting the trial court's finding that the Bank's officers knew the facts of the transaction at the time it occurred.

The first of these findings, supplied on appeal, had never been suggested in the case, either by the court below or by counsel. The second is shown by the dissenting opinion to be unsound. As to the third (concerning laches), plaintiffs did argue on the appeal that our evidence of what was known to the Bank in 1919 did not prove that the officers then had notice of the facts complained of; but this contention obviously ignored (as does the reasoning of the court below), the admitted fact that the burden was on plaintiffs to plead and prove lack of discovery by the Bank at any time during the fifteen year period.

The course taken by the court below should be contrasted with the view expressed in the opinion of this Court in *Indiana Farmers' Guide Publishing Co. v. Prairie Farm Publishing Co.*, 293 U. S. 268, 281, where the court said:

> "Respondents had opportunity here to show that, although given on untenable grounds, the judgment below is right and should be affirmed. And, if by the record they could so demonstrate, this court, *if satisfied beyond doubt that it could do so without prejudice to petitioner,* properly might refrain from reversal. * * * Certainly, in the absence of a claim on their part that, conceding the errors exposed by this opinion, the judgment is right, we will not examine the record to discover grounds to sustain it. Cf. *Chicago M. & St. P. Ry. Co. v. Tompkins,* 176 U. S. 167, 179. *Hammond v. Schappi Bus Line,* 275 U. S. 164, 170 et seq. * * *
>
> "The judgment of the Circuit Court of Appeals should be reversed and the case remanded to the District Court with directions that petitioner be granted a new trial." (Emphasis added.)

The two cases cited in the above quotation were equity appeals wherein this Court ordered a new trial because of the insufficiency of the findings.

We submit that for this reason alone, the decree of the trial court should have been reversed.

We submit that the judicial process does not allow the presumption of regularity to be expanded so as to mean that the very decision itself of the trial court is

presumed to be correct, even though the grounds upon which it rests are shown to be unsound, wherefore the judgment should be affirmed if a view of facts can be stated which might have been held to be supported by some evidence if the trial court had found them to be true.

We submit, that the obviously untenable proposition just stated is implicit in the process by which the judgment was affirmed by the court below.

In the next section we show that the view of the facts put forward by the court below is not supported by the record, even if it be given the weight which is properly accorded only to the findings of trial courts.

POINT IV.

ON THE MERITS, NO FRAUD IS SHOWN

Although the trial court's decree against Petitioner was affirmed below, this is not a case within the rule that "concurrent findings of the courts below will be accepted by this Court unless clear error is shown". (*Radio Corp. v. Radio Laboratories,* 293 U. S. 1, 6)

On the contrary, the view of the facts taken in the court below differs radically from that of the trial court, as shown above.

We shall show, moreover, that (as we submit) the facts upon which the lower courts do agree, demonstrate the unsoundness of the judgment.

The Charge Made.

The basis of the suit and the decree is the charge that in 1919, Petitioner received an interest in the

partnership in exchange for aiding the Bardes to obtain loans from the Bank, of which Petitioner was president.

Preliminary Considerations.

Preliminarily the following circumstances should be noted:

1. There is no evidence, nor any attempt to show, that there was an express agreement or understanding between Petitioner and the Bardes that Petitioner should receive this interest or anything else, for the loans. Both courts agree that there was not. (R 187, 906)

2. There is no evidence or attempt to show that Petitioner did anything more toward the granting of the loans by the Bank than to recommend them to the Bank's Finance Committee. That Committee (the Petitioner not participating) approved the loans in the usual course. There is no evidence that Petitioner dominated the Finance Committee or the Board of Directors, or any member of either, or that he put pressure of any kind on them or any of them. Whatever weight his recommendation may have had in fact there is nothing in the evidence concerning it, and no suggestion anywhere in the evidence that it was abnormal or improper in any manner or degree.

The Bardes were Old Customers of the Bank, and their Credit was Excellent.

We come now to the circumstances surrounding the granting of the loans. As we now show, no

imaginable suspicion arises out of the physical fact that these loans were made.

Prior to the transaction here in question, the Barde corporation had done much business with the Bank, having an unsecured line of credit of over $100,000. (R 451) The total of their loans from the Bank during the six months immediately preceding December, 1919, was $138,122.33, which had been reduced to $8,653.45 at the time of the loans complained of. (R 451) Earlier, the Barde corporation had done business with another bank whose president was a member of the Anglo Bank's Finance Committee which passed on the loans. (R 618)

The Bardes were engaged, in Portland, Oregon, in business through their corporation, M. Barde & Sons, Inc., the borrower. (R 176) Their corporation, the borrower, on December 23, 1919, had a net worth of $750,000 (R 607), which fact was known to the Bank at the time it granted the loans. (R 625)

The terms of the loans complained of (6% demand notes) were more favorable than was the general rule in respect of such loans at the time. (R 605, 626-8)

The loans were secured by a pledge of something over $200,000 worth of Liberty Bonds (R 178), and in the language of the trial court, were "fully protected". (R 186)

The making of these loans by the Bank was therefore perfectly natural, and in no way a suspicious circumstance in itself.

The loans being natural, and indeed unusually desirable loans, it was also perfectly natural for Petitioner to recommend them to the Finance Committee.

Although the loans were not to the partnership in which the Petitioner had a half interest, but to Petitioner's partners, they would have been entirely proper if made directly to the partnership, or to Petitioner himself.

Such loans were perfectly lawful, and very common.[1] (R 626-7, 649) Loans to officers of member Banks of the Federal Reserve System were first limited in 1933, the new provision allowing renewals or extensions of existing loans up to 1939, and allowing loans directly to partnerships so long as officers of the Bank do not have more than a half interest. (48 Stat. 182; 49 Stat. 375; 49 Stat. 716; 52 Stat. 223; 53 Stat. 842; 12 U.S.C. §375a)

In 1 *Michie on Banks and Banking,* (Perm. Ed.) p. 145, the rule is stated:

> "In the absence of the statute forbidding loans to officers of the bank, there is no moral or legal turpitude involved in a *bona fide* loan obtained from the bank with the knowledge and consent of the directors."

And see: *Gallin v. National City Bank,* (1934) 273 N. Y. S. 87, 97; *National Bank of Commerce v. Na-*

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(1) See Proceedings of the Subcommittee of the Banking and Currency Committee of the United States Senate, 74th Congress, 1st Session, pp. 79-100.

tional Bank of Missouri, (1878) 30 Fed. Cas. 1121, 1122; *Blair v. First National Bank,* (1877) 3 Fed. Cas. 577, 580; *Witters v. Sowles,* (1887) 31 F. 1; *Briggs v. Spaulding,* (1891) 141 U. S. 132; 3 *Fletcher Cyclopedia of Corporations* (Perm. Ed.), Sec. 955, p. 334.

The undisputed fact is that Petitioner did not keep his relation or interest in this matter a secret. On the contrary, as shown at length above, the essential facts (namely, that Petitioner was a partner in the venture in which the funds were to be used), and indeed most of the details, were common knowledge in the Bank, being known to the officers who testified, and to many others now dead. (R 190, 313, 429, 604, 611, 620, 624, 629, 644, 652, 678, 700)

The Vital Question.

The fact is, then, that the recommendation of these loans by Petitioner (which was his only act of participation as a bank officer in connection with them), and the granting of the loans by the Bank were, in the circumstances, perfectly natural, and furnished the court below no ground for suspicion of wrongdoing.

It is, of course, nevertheless true that if Petitioner in fact received his interest in the partnership in exchange or as consideration for the loans or for his recommendation of the loans, he would be liable in this suit.

The vital question therefore is this: Is there sufficient or any evidence to support an inference of fact that Petitioner did receive an interest in the

partnership for the loans or for his recommendation of the loans to the Bardes?

The Proof, Findings and Admissions are that the Partnership was Formed Before Petitioner Learned that any Loans were Needed or Desired.

The proposition just stated in the heading is shown beyond question. In the first place, Petitioner testified unequivocably that he did not learn of the desire of the Bardes to borrow money, whether from the Bank or elsewhere, until after the partnership had been formed. (R 675) Neither court has questioned Petitioner's credibility as a witness, and indeed, his testimony on this specific question was in terms accepted by the trial court in its opinion which reads in part as follows:

> "After full investigation Herbert Fleishhaker agreed to become a partner in the deal. 'When it came to putting up the money,' testified Herbert Fleishhacker, 'they asked me if they could borrow, if the firm of M. Barde & Sons could borrow some money from the bank.'" (R 177)

The substance of this passage from the court's opinion was carried into the findings: "After having agreed to become an equal partner in said enterprise as aforesaid, the defendant Fleishhacker was advised by the said Bardes" that the sums later borrowed would be required (R 298); and was repeated in the opinion of the court below. (R 901)

The same fact was admitted by counsel for the plaintiff. The following are excerpts from plaintiffs'

briefs in the trial court, which excerpts are in the record. (R 707, ff)

> "Admitted Facts. The following pertinent facts, we [plaintiffs] believe, stand undisputed in the record. * * * Herbert Fleishhacker agreed to enter the deal as an equal partner (that is, on a basis of one-half to Fleishhacker and one-half to the two Bardes) if investigation convinced him the deal would be profitable. * * * After the deal had been investigated and approved and Fleishhacker had agreed to go in as an equal partner, he, Fleishhacker, was advised by the Bardes that they would have to borrow the necessary money. They applied to Herbert Fleishhacker for a loan from the Anglo Bank. Fleishhacker recommended to the finance committee of the bank the approval of loans of $325,000, knowing this money was to be used to launch the venture in which he had a half interest." (R 708-9)

> "That Fleishhacker, being informed by his partners that the necessary cash would have to be raised by loans, cooperated in procuring the loans from the bank of which he was president, admits of no question. He did this with full knowledge that the funds coming from the bank would be used in this identical enterprise, for his benefit and his profit." (R 715)

We submit that in these circumstances the conclusion reached below, namely, that Petitioner received his interest in the partnership in exchange for his recommendation of the loans to the Bardes is not supported by the evidence.

We turn now to the processes of reasoning whereby the courts below nevertheless reached a conclusion adverse to Petitioner.

Reasoning of the Trial Court.

Having found that Petitioner did not learn that the Bardes would desire to borrow money (whether from the Bank or elsewhere) until after the partnership agreement had been made (R 177), and that there was no express agreement that Petitioner should receive an interest in the venture for the loans (R 187), the court said:

> "In the Downey case the president of the bank agreed to furnish the money required upon the expressed condition that he should become personally interested to the extent of one-sixth of the profits of the land transaction, while here there was no expressed condition for participation in the profits. This presents the question, Do the facts here justify an inference that a part of the consideration for the loans to the Bardes was an agreement that Fleishhacker should participate in the profits of a deal financed from the funds of the Anglo Bank?" (R 187-8)

The court answered this question as follows:

> " * * * upon the recommendation of Fleishhacker, the Anglo Bank loaned the money which made the venture possible. * * * The business was profitable, Fleishhacker's share thereof amounting to about $300,000. Under these circumstances may it not be said that Fleishhacker, president of a national bank, received a thing of value * * *

for procuring from his bank a loan to launch the venture?" (R 189)

Upon this basis the court concluded "a part of the consideration for the loans" was Petitioner's interest in the partnership. (R 196)

It is, we submit, obvious that the ground for the trial court's decision is thus shown to be, that since the loan by the bank contributed to the success of the venture, and since that loan was made upon the recommendation of Petitioner, those circumstances require the conclusion that Petitioner "received a thing of value * * * for procuring from his Bank a loan to launch the venture."

It is apparent, however, that the trial court's conclusion does not follow from the facts upon which it rests.

The trial court has confused consideration with contributing circumstance.

It is perfectly true (as with every loan to a bank officer or to a partnership or corporation in which he is interested) that the proceeds of the loan contributed to the success of the venture. The vital point is, however, that it is not a wrong—moral, legal or other—for a bank officer to recommend, or for a bank to grant, a loan to persons with whom the bank officer is associated.

We ask this Court to examine the trial court's opinion in full, in order that the Court may have no doubt that the foregoing accurately states the untenable ground of the trial court's decision. (R 175)

Reasoning of the Court below.

The court below paraphrased the findings of the trial court, in part as follows (R 901):

> "Following were the facts as found by the trial court: * * * They [the Bardes] invited Herbert Fleishhacker to join in the proposed enterprise. The Bardes and Fleishhacker conducted independent investigations and decided that the venture would be a profitable one. Thereupon, about December 1, 1919, the Bardes and Fleishhacker agreed to join in the enterprise on the basis that Fleishhacker was to be an equal partner with the two Bardes, namely, a one-half interest to Fleishhacker and one-half to the Bardes.
>
> "After having agreed to become an equal partner, Fleishhacker was advised by the Bardes that $250,000 was required to launch the enterprise, such amount being necessary to qualify the bid, and that, if the bid was successful, an additional $250,000 would be needed."

The court then stated Petitioner's argument that since Petitioner had entered into the venture (and thus received his interest therein) before he learned that the Bardes desired to borrow, it followed that the loans could not have been consideration for that interest. The court disposed of this argument as follows (R 906):

> "The argument is based upon what we regard as an unwarranted interpretation of the findings as a whole, and it is not borne out by the evidence. * * * Prior to the time it became necessary to

> raise the money there had been no definite contract finally determinative of the rights and liabilities of the parties in the venture. All that seems to have been clearly decided was that Fleishhacker was to go in with the Bardes upon a general fifty-fifty basis. The details were uncertain. Necessarily, the entire matter remained at large until the terms of the Shipping Board were finally ascertained and the parties were faced with the specific problem of meeting them."

The trial court's opinion and findings quoted above show plainly that the trial court had no such idea, and as shown, the idea is contradicted by all the relevant evidence.

The court below then says (R 906):

> "It seems plain that Fleishhacker's interest in the venture was proffered him, in substantial measure at any rate, in exchange for anticipated services in the procurement of loans. Fleishhacker must be deemed to have acceded to this condition when his tentative understanding with the Bardes ripened into a definite working contract."

The view of the facts thus adopted by the court below may be summarized as follows:

1. The Bardes offered to enter into an equal partnership in this venture with Petitioner, but concealed the fact that they would want to borrow their contribution to the necessary capital later on.

2. After independent investigation the parties agreed to proceed as equal partners, Petitioner on the one side and the two Bardes on the other.

3. Thereafter when it came to putting up the money, the Bardes informed Petitioner that they desired to borrow part of their contribution to the venture, and asked Petitioner if they could borrow it from the Bank.

4. At this point (the court seems to say), Petitioner could and should have withdrawn. Since the partnership agreement (says the court) was still tentative, because the details were still uncertain, it follows that Petitioner, by recommending the loans to the Bank (instead of refusing to, or withdrawing from the venture), "must be deemed to have acceded" to the theretofore undisclosed intention of the Bardes to proffer Petitioner an interest in the venture "in exchange for anticipated services in the procurement of loans".

There is No Ground for the Conclusion that the Partnership Agreement was Tentative and the Trial Court Found the Contrary.

It is not disputed that prior to any intimation that the Bardes desired to borrow money, the parties had, after independent investigation of the venture, agreed that they would proceed, and that their rights and liabilities should be as follows:

1. The venture would require approximately $1,000,000, in cash or credits (R 176-77, 363-4, 367-8, 663, 666, 669);

2. The Bardes would put up $500,000, in cash if necessary and required (R 665-6, 669);

3. Petitioner would put up $500,000, either in cash, in securities, or in the form of a bond if the Shipping Board would accept a bond (R 669); and

4. Any profits realized would be divided equally, between the Bardes on the one hand and Petitioner on the other. (R 665-6, 669)

The court below does not question these physical facts, but argues that notwithstanding them, the agreement was only tentative, because the details were uncertain.

The contrary is, we submit, clear. In the first place, there is no ground upon which it could be argued that the trial judge found as a fact, or concluded as a matter of law, that the partnership agreement was not a binding agreement. Indeed, as we have shown, the trial court's finding that the partnership agreement was made, is unqualified, and therefore contradicts the conclusion reached by the court below.

The truth is that most oral partnership contracts (which are sustained as sufficiently certain), are far less clear and definite than the agreement here, the making of which is not disputed. See *Carpenter v. Hathaway,* 87 Cal. 434; *Caldwell v. Western Development Co.,* 54 Cal. App. 776; *Watson v. Kellogg,* 129 Cal. App. 592; *Goldsmith v. Sachs,* 17 Fed. 726.

It is, of course, not true that the binding effect of the partnership agreement was impaired by the fact that the manner in which the partners would perform

their obligations was not specified.[1] They seldom are in oral contracts of partnership, and generally cannot be at the time of the contract. (See the cases cited above, particularly *Goldsmith v. Sachs* and *Watson v. Kellogg.*)

We submit that for the court below thus to resort to a strained inference (contrary to the trial court's view of the facts), in order to sustain a charge that a fraud was committed fifteen years before action brought, is not only unfair, but contradicts established principles concerning the exigencies of proof of fraud.

Every essential step in the chain of suspicious circumstances, built up by inference by the court below, is without support in the evidence. There is no suggestion anywhere to support the court's theory that the Bardes planned to obtain the loans by first getting Petitioner into the venture and then disclosing their need to borrow. Even if there were such evidence, it would not affect Petitioner. Unless it is fair to infer from the evidence that when Petitioner was informed that the Bardes desired to borrow, he was thereby led to believe that he had been invited into the venture for the very purpose of getting loans, the fact that he had been, even if it were a fact, would not affect his

---

(1) This assumes the court below correctly stated that "the details were uncertain." But such is not true, as the only indefiniteness as to manner of performance was the alternative of providing cash of $500,000 or an equivalent thereof in the form of securities or an indemnity (surety company) bond.

good faith. In any event there is no evidence whatever that any such plot was devised, and no intimation that the trial court had any such idea.

Petitioner Contributed Half the Capital.

Both courts below asserted, and treated as a suspicious circumstance, the proposition that (apart from his recommendation of the loans) Petitioner contributed little or nothing to the venture. Thus the trial court said:

> "None of the parties personally contributed any money, but, upon the recommendation of Fleishhacker, the Anglo Bank loaned the money which made the venture possible. * * * Fleishhacker received one-half of the capital stock without paying a dollar of his money for it." (R 189)

Similar language was used by the court below:

> "While Fleishhacker arranged for and guaranteed a faithful performance bond of $500,000 for the Corporation, between him and any possible liability to the surety company lay a cash deposit of at least $400,000. He personally put no money into the enterprise and took small financial risk." (R 908)

It is, we submit, plain that these statements play with words and fail to apply elementary principles of finance. As has been shown, the agreement was that the Bardes should supply half the capital, in cash if necessary, and that Petitioner should supply the remaining half, in cash, securities or a bond as required by the Shipping Board. (R 177, 666, 669, 704) To say

that Petitioner did not put any "money" into the venture is to ignore every-day and universally understood practices. When people invest they do not take currency out of a strong box—they normally supply credit. The California Supreme Court characterized such use of language and disregard of substance as a "paltering with words". (*Grigsby v. Schwarz,* 82 Cal. 278, 281-82)

In this case, all concerned supplied credit. The Bardes obtained their contribution by using their credit to borrow. Petitioner made his contribution by supplying his credit more directly to the venture, i.e., by supplying, not money in the sense of legal tender, but money's worth. The fact that his contribution was identical with actual cash is shown by the agreement itself, under which he was to supply cash, securities, or a bond if the Government would accept a bond. The credit required to provide a surety company indemnity bond of $500,000 as security for a contract involving "the purchase of surplus steel of the value of about $40,000,000" (to use the trial court's words, R 176), is as great as that required to borrow an equal amount.

The risks incurred by Petitioner on the one hand and the Bardes on the other, were identical. The case is of course no different as to risks assumed from what it would be if the Bardes had borrowed from some other lending institution. Their immediate risk was, that should the venture not be profitable, they would have to pay the notes with which they obtained their contribution. Petitioner's immediate risk was

that if the venture should not prove profitable he would become liable to indemnify the surety company on the bond. So long as all or part of the $400,000 cash deposit (made with the Bardes' contribution) was still avaliable, it might be that would be resorted to before recourse was had to the bond.

But the vital point is that the ultimate risks assumed by the parties were identical. The opinions ignore basic principles of partnership law; and the like rules of contribution between co-sureties. It was the majority rule at common law, including California, as it is the rule in California now (Civil Code, Sec. 2412), and elsewhere under the Uniform Partnership Act, that final settlement between partners requires:

1. Crediting each of them with his capital contribution;

2. Crediting or charging each partner with his share of the profits or losses; and

3. Such payments out of the partnership funds, or from one partner to another, as will produce the effect that the net profit or loss realized by each partner is in proportion to his share in the venture.

> " * * * For example, suppose A, B and C have contributed respectively $10,000, $5,000, and $2,000 to the firm's capital of $17,000, and share profits equally. On dissolution, after paying debts there remains $5,000, a capital loss of $12,000. Sharing this equally means a debit to each of $4,000. A would receive $6,000, B would receive

> $1,000, and C would pay in $2,000 to meet the deficiency * * * ". (*Crane on Partnership,* p. 281)

See, also, *Sherwood v. Jackson,* 121 Cal. App. 354; 20 *Cal. Jur.* 849 et seq.; *Crane on Partnership,* §§65, 90.

In this connection it is significant that Petitioner's liability for capital contributions was recognized in the manner in which the Bardes' loans at the Bank were paid off. The funds for this purpose were provided by the Steel Corporation, but as each payment was made, half was charged on its books to the Bardes and half to Petitioner. In the same manner Petitioner was charged with one-half of the payments made by the Steel Corporation in discharge of the Central Bank loans to the Bardes. (R 407-10, 432)

Likewise, under the law of contribution between cosureties, the fact that resort might have first been had to the cash guaranty fund (although not so required by the Shipping Board contract) would not in the least have affected liability to contribute to the Bardes on account thereof.

In every imaginable contingency, therefore, Petitioner's risks were identical with those of the Bardes. If the venture had lost the $500,000 put into it in cash, but no liability had accrued on the bond, then Petitioner would have been obligated to pay to the Bardes the sum of $250,000.

It is perhaps possible to surmise that the risk of the Bardes was more immediate than the risk of Petitioner, i.e., that if the venture had failed the Bardes

would have had to pay their notes prior to the time that Petitioner would have had to respond on his indemnity bond. It is, however, thoroughly unreasonable to conclude on that ground that Petitioner's contribution was substantially less than the contribution made by the Bardes. As a matter of fact, Petitioner's risk continued beyond the time that the immediate risk of the Bardes was discharged. Their notes were paid in four months; Petitioner's bond was outstanding until the contract with the Shipping Board was terminated.

Conclusion on the Merits.

We respectfully submit that the circumstances of the transaction put forward in this case as supporting an inference of fraud furnish no reason even to suspect that fraud was present.

It follows that the charge of fraud (alleged to have been committed fifteen years before suit brought) is unsupported; and that the action of the court below, in finding the evidence sufficient to sustain the charge, contradicts long established rules (a) that fraud is never presumed; (b) that the presumption against fraud approximates in strength that of innocence of crime; and (c) that if two inferences equally susceptible of being drawn from proved facts, one favoring fair dealing and the other favoring corrupt practice, it is the express duty of the court to draw the inference favorable to fair dealing.

The decision opens the door to dangerous and undesirable speculation in stale charges of fraud. See *Conrad v. Nicoll,* 4 Pet. 291, 296-7, 310.

CONCLUSION

The following propositions are, we submit, supported by this petition and brief:

1. The rule announced below emasculates Equity Rule 27 (now Rule of Civil Procedure 23(b)) and the rule of substantive law embodied therein, and opens the federal courts to (a) almost unlimited litigation by stockholders who seek to substitute their judgment concerning corporate policy for that of the Board of Directors, and (b) stockholders' suits brought in bad faith in order to harass the corporation into concessions concerning unrelated matters.

2. The decision opens the federal courts to almost unlimited speculation in stale charges of fraud, by holding that fifteen years of wholly unexplained delay is not laches.

3. The trial court signed, without change, findings prepared by counsel which are inconsistent with the court's own opinion in important particulars, and the court below not only gave full effect to these findings but went further and drew strained inferences therefrom to sustain the decision.

4. The opinions below plainly violate accepted principles concerning the exigencies of proof of fraud, particularly in cases where, as here, the charge is brought forward fifteen years after the event, most of the persons who could have testified concerning the matter being dead.

5. The evidence does not show that Petitioner received a bribe or bonus for procuring a loan of

the Bank's funds, or that he committed any breach of his fiduciary duty to the Bank.

It is submitted that the Writ of Certiorari should be granted, the decree of the court below reversed, and the bill directed to be dismissed.

Respectfully submitted,

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Counsel for Petitioner.

JOHN FORD BAECHER,
EVAN HAYNES,
Of Counsel.

In the

Supreme Court of the United States

OCTOBER TERM, [redacted] 1940

No. 181.

HERBERT FLEISHHACKER,

Petitioner,

vs.

LUCIEN BLUM, EDMOND LANG, ELIZABETH LANG, RENE FOULD, ESTHER FOULD, MAX LAZARD, ROGER HAAS, ANDRE HAAS, LUCIE EMILE LEWYLIER, S. A. JOHANESSON, G. O. HOFFMAN and HENRY LEON,

Respondents.

APPELLEES' BRIEF IN RESPONSE TO PETITION FOR WRIT OF CERTIORARI.

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Official Reports of Opinions Below.

The opinion of the trial court is reported in 21 Fed. Supp. 527. The opinion of the Circuit Court of Appeals for the Ninth Circuit is reported in 109 Fed. (2d) 543.

Statement of the Case.

Pursuant to Rule 27, paragraph 3, of this Honorable Court, we limit our statement of the case to a correction of inaccuracies and omissions in the statement of the petitioner. Parenthetical references are to the pages of

the record, except when preceded by the symbols "Petn." or "Br.", which refer, respectively, to the petition for certiorari and the petitioner's brief in support thereof. The Anglo-California National Bank of San Francisco is referred to throughout this brief as the Bank.

This is a suit in equity to recover for the Bank profits received by the petitioner, its president, for causing the Bank to loan funds to finance the business venture from which the profits arose. This venture consisted in purchasing and reselling a large quantity of steel owned by the United States Shipping Board Emergency Fleet Corporation. Petitioner caused the Bank to advance $325,000.00 to L. B. Barde and J. N. Barde, upon two notes executed by M. Barde & Sons, Inc., one for $250.000 dated December 16, 1919, and the other for $75,000 dated December 21, 1919. The record shows that the Bardes simply signed the papers required by petitioner to get the money necessary for the financing which petitioner had undertaken.

On the trial of the cause counsel for petitioner, in oral argument, stated the issue in the case to be as follows (706):

> "If Your Honor feels that Fleishhacker solicited or accepted in any degree whatever as a consideration for lending the funds of that bank anything of value the judgment must be for the plaintiff."

Counsel for appellees took the same view and contended that the record showed that petitioner undertook to finance the venture in order to obtain a half interest in it and that part of the consideration for the lending of the funds was the interest received by petitioner.

The trial judge, in a written opinion, said (196):

> "After a consideration of the whole case, I find that Herbert Fleishhacker violated his trust to the bank and its stockholders; that a part of the consideration for the loans of the Anglo Bank to the Bardes was the participation by Herbert Fleishhacker with them in the profits of the steel deal; that Herbert Fleishhacker made a private profit for himself in the discharge of his official duties."

And in its written findings the trial court found as follows (300):

> "Part of the consideration for the said loans to the Bardes of the funds of the defendant bank was an agreement between said Bardes and said Fleishhacker that said Fleishhacker should participate in the profits of the enterprise to be financed by such funds of the defendant bank."

On appeal, the suit being in equity, the Circuit Court of Appeals again considered the weight and effect of the evidence, and after reviewing the same, concluded (909):

> "But the essential verities of the situation cannot be explained away, and when all is said there remains an ineradicable conviction that Fleishhacker used his position as president of the Bank as a means of securing emoluments personal to himself."

The respondents, stockholders of the Bank, are citizens and residents of France. Petitioner's assertion that their purpose in instituting this suit was to obtain evidence to use against the Bank in other litigation (Petn. 3) is an inference which cannot properly be drawn from the evidence (459). Nine of the twelve respondents had no interest in this other litigation (586).

The record shows that in September, 1919, M. Barde & Sons Inc. owed the Bank $111,000 (451), but there is no evidence to support petitioner's assertion (Petn. 3, 5) that it had an *unsecured* line of credit in that or any other amount. Neither is there any evidence to support the contention (Petn. 3) that on December 23, 1919, the company had a net worth of $750,000. The files of the Bank contained a statement dated January 29, 1920, showing assets of $750,000 as of December 23, 1919, but this statement (607) did not purport to show the company's obligations to the Bank or any other liabilities, and it was admitted that it was not a statement upon which the Bank could make a loan (635). In fact, J. N. Barde testified (368):

> "We did not have a line of credit with the Anglo Bank or any other bank of a half a million dollars."

Petitioner also states (Petn. 2, 5), as did the trial court in its opinion (but not in its findings), that the loans in question were secured by over $200,000 in Liberty Bonds. The Bank's records, however, show that the notes were carried as unsecured items (613). The court found that the Liberty Bonds were delivered by the Bardes to the Bank *or to petitioner* (300)—in the latter event, obviously, to secure him against loss in the enterprise.

The assertion is made (Petn. 5) that the Bank's finance committee "authorized" the loans. The record shows that the Bank forwarded the first $250,000 to the Bardes on December 19, 1919, and the remaining $75,000 on December 22, 1919 (451), but it was not until December 24,

1919, that the loans were approved by the finance committee (618). It will be noted that the $75,000 note was executed on a Sunday, at petitioner's residence, and the money left the Bank the next day. The minutes of the finance committee merely show that on the 24th forty-two loans were approved by number and that the numbers stated included those given the two loans to the Bardes (601).

Many of the petitioner's statements, referred to as facts found by the trial court, are taken from the court's opinion, rather than its findings of fact. This, of course, is improper. An opinion is not a finding of facts (*Interstate Circuit, Inc. v. United States*, 304 U. S. 55, 82 L. ed. 1146), and where the trial court makes separate findings the opinion cannot be regarded as a finding of any fact whatsoever.

Rickard v. Thompson (C. C. A. 9), 72 Fed. (2d) 807, 910;

Utah Commercial & Savings Bank v. Fox, 44 Utah 323, 140 Pac. 660.

We do not agree with many of the conclusions presented as facts in petitioner's "Summary" (Petn. 8-10), but these can more properly be discussed in considering the sufficiency of the evidence to support the finding that petitioner used his position as president of the Bank to secure emoluments personal to himself. Inasmuch as this evidence is necessary to complete the Statement of the Case, we shall depart from the order of presentation adopted by petitioner and proceed at once to a discussion of the same.

ARGUMENT.

I.

Certiorari Should Not Be Granted Because of the Alleged Insufficiency of the Evidence to Support the Judgment on the Merits.

The fourth reason assigned by the petitioner for granting certiorari is stated as follows (Petn. 28):

> "The court below erred in finding petitioner received a bonus for a loan of the Bank's funds and received a profit for which he must account to the Bank."

This contention raises an issue as to the sufficiency of the evidence, an issue already twice decided in favor of the respondents. We respectfully submit that it should not be necessary to review the evidence a third time. This Honorable Court, in *Magnum Import Co. v. Coty*, 262 U. S. 159, 163, 67 L. ed. 922, 924, said:

> "The jurisdiction to bring up cases by certiorari from the circuit courts of appeals was given for two purposes: first, to secure uniformity of decision between those courts in the nine circuits; and, second, to bring up cases involving questions of importance which it is in the public interest to have decided by this court of last resort. The jurisdiction was not conferred upon this court merely to give the defeated party in the circuit court of appeals another hearing."

And the court has repeatedly declared that certiorari is not warranted merely to review the evidence or the inferences drawn therefrom:

General Talking Pictures Corp. v. Western Elec. Co., 304 U. S. 175, 178, 82 L. ed. 1273, 1275;

United States v. Johnston, 268 U. S. 220, 227, 69 L. ed. 925, 926.

Counsel for petitioner, in discussing the sufficiency of the evidence, completely ignore that which tends to support the judgment. It must be remembered that, although the petitioner had agreed to join with the Bardes in the steel venture before anything was said to him about borrowing money, the entire enterprise was conditional upon acceptance by the Shipping Board of the bid which the Bardes proposed to make. We know, also, that the bid was not even presented until after the Bardes had made known to the petitioner that they would have to borrow money, for the first $250,000 advanced by the Bank was used as a deposit to qualify the bid. All this is conceded by the petitioner (Petn. 4); yet the argument is made that petitioner's activity in causing the Bank to make the loans could not have been intended as a consideration for his interest in the venture because that interest had been promised him before the loans were first mentioned. The answer, of course, is that petitioner had been promised a one-half interest in the venture *if the bid was accepted,* and when the Bardes informed him that they would have to borrow $250,000 to qualify their bid and another $250,000 immediately upon its acceptance, the petitioner knew that his share in the venture was conditional also upon the raising of this $500,000.

It is significant that at this time petitioner did not merely suggest that the Bardes attempt to borrow the money, but said "right off" (367) that "he would attend to it and get it" (370). This conversation, between petitioner and J. N. Barde, took place, not in the Bank's premises, but at the petitioner's residence (363). That petitioner really directed the financing of the venture ap-

pears from Exhibit 24 (638), a letter dated December 16, 1919, from J. N. Barde to the petitioner, transmitting the first note for $250,000, which reads as follows:

> *"In accordance with your wishes regarding Eastern Deal,* writer is enclosing note in the sum of $250,-000.00 payable on demand and has instructed Mr. L. B. Barde, now in New York, to see the Guarantee Trust Company and do likewise.
>
> *Hoping we have complied satisfactorily to your wishes in the matter,* we are
>
> Very truly yours,"

Also, we have in evidence a telegram dated December 19, 1919, sent from Portland by J. N. Barde to the petitioner, reading as follows (698):

> "Just received following wire from L. B. Barde Pennsylvania Hotel New York Wire received arrangements suggested satisfactory to me *Arrange with Herbert for additional credit here of Two Hundred Fifty Thousand* covering One hundred fifty thousand balance payable on signing of contract and one hundred thousand dollars working capital Tell Herbert I have asked Parker to act as his representative on trade stop *Writer will be with you Sunday morning* and advise with you and *listen to your suggestions relative to handling this deal.*
>
> JACK."

At the meeting on Sunday, December 21st, J. N. Barde signed two notes, one to the Bank for $75,000 (373) and another to the Central National Bank of Oakland for $175,000 (374). This latter loan the petitioner obtained for the Bardes by telephoning the president of the Oakland bank, and it was made upon petitioner's personal guaranty (682).

After the Shipping Board accepted the Bardes' bid, they organized the Barde Steel Products Corporation to handle the enterprise. One-half of its stock was placed in the names of petitioner's nominees for his benefit. It is highly significant that petitioner admitted that one of the considerations for which these shares were issued to him was his guaranty of the $175,000 note to the Oakland bank (446-7). This admission, which was stressed in the opinion of the Circuit Court of Appeals (907), is not even mentioned in petitioner's brief. It establishes beyond dispute that the consideration furnished by petitioner was not finally determined until *after* the Bardes had advised him they would have to borrow money. The sum required was $500,000, and if petitioner's efforts in obtaining the $175,000 was part of the consideration for his share in the venture, then his efforts in securing the remaining $325,000 from the Bank of which he was president must also have been a part of the consideration which he furnished for that share. As stated by the Circourt Court of Appeals, "the transactions are of one piece."

It is quite evident that the agreement on the part of the Bardes that petitioner should have a half interest in the venture was express (366-704). Also, the agreement of petitioner to procure the necessary $500,000 was express (367). The only factor which was not expressed in so many words was that the promise to give petitioner the half interest in the venture was in consideration for his procuring the $500,000. The same was true in the leading case of *Farmers & Merchants Bank v. Downey*, 53 Cal. 466, 31 Am. Rep. 62, which is strikingly similar on its facts. The reported opinion in that case states that the bank's officers agreed to furnish the funds "upon condi-

tion that they should become personally interested in the sale to be made"; but an examination of the transcript on appeal in that case, No. 6051 in the files of the clerk of the California Supreme Court, shows that the condition was never expressed. In that case, as in this, the offer of an interest in the venture originated with the borrowers. A written agreement was prepared which made no mention of the connection of the defendants with the bank or of their activity in obtaining the loans. Indeed, the defendant Downey actually invested some of his own funds in the venture. The loan made by the bank was adequately secured and had been almost entirely repaid, with interest, when the action was filed. Yet the California court said of the defendants:

> "The law will not permit them to make a private profit for themselves in the discharge of their official duties; and, as observed by the Court of Appeals of the State of New York, in *Bow v. Brown*, 56 N. Y. 288, 'When agents and others, acting in a fiduciary capacity, understand that these rules will be rigidly enforced, even without proof of actual fraud, the honest will keep clear of all dealings falling within their prohibition, and those dishonestly inclined will conclude that it is useless to exercise their wits in contrivances to evade it.'"

A classic statement of the principle involved is that of Mr. Justice Cardozo in *Meinhard v. Salmon*, 249 N. Y. 458, 164 N. E. 545, 546:

> "'A trustee is held to something stricter than the morals of the market place. Not honesty alone, but

the punctilio of an honor the most sensitive, is then the standard of behavior. As to this there has developed a tradition that is unbending and inveterate. Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty by the "disintegrating erosion" of particular exceptions. Only thus has the level of conduct for fiduciaries been kept at a level higher than that trodden by the crowd. It will not consciously be lowered by any judgment of this court.'"

Much more could be said as to other evidence tending to support the judgment on the merits, but to do so would seem to be unnecessary. Both the trial court and the Circuit Court of Appeals concluded that the stock issued to the petitioner and the profits derived by him from the venture were received by him in consideration for procuring loans of the funds necessary to launch the enterprise. It is well established, particularly in equity suits, that when the findings of the two lower courts are in agreement, they will not be disturbed unless plainly without support in the evidence.

General Talking Pictures Corp. v. Western Elec. Co., supra;

Alabama Power Co. v. Ickes, 302 U. S. 464, 477, 82 L. Ed. 374, 377;

United States v. O'Donnell, 303 U. S. 501, 598, 82 L. Ed. 980, 984.

II.

Certiorari Should Not Be Granted Because of Alleged Insufficiency of the Evidence to Justify Equitable Relief at the Instance of Respondents.

The first reason assigned by counsel for petitioner for allowance of the writ is stated as follows (Petn. 20):

> "The court below has decided a federal question in a way conflicting with applicable decisions of this court."

The so-called "federal question" referred to, we find upon examination of the brief, is the alleged insufficiency of the evidence to show compliance with certain conditions precedent applicable to stockholders suits. But this is not a "federal question" within the meaning of paragraphs 5(a) and (b) of Rule 38 of this Honorable Court. Rule 38 refers to such questions as are reviewable under Section 237b of the Judicial Code (*Stoll v. Gottlieb,* 305 U. S. 165, 167, 83 L. Ed. 104, 106)—that is, questions as to "the validity of a treaty or statute of the United States", or "the validity of a statute of any State on the ground of its being repugnant to the Constitution, treaties, or laws of the United States; or where any title, right, privilege, or immunity is specially set up or claimed by either party under the Constitution, or any treaty or statute of, or commission held or authority exercised under, the United States."

Here there is no doubt that the bill of complaint complied with Equity Rule 27. The petitioners objection is that the allegations were not proved and that the *evidence* is, according to his contention, insufficient to justify a court of equity in granting relief which the directors refused to seek. This is in no sense a "federal question."

And as already observed, this Court has declared repeatedly that it does not grant certiorari to pass upon the evidence, especially in cases such as this, where both lower courts are in agreement as to its sufficiency.

There is no suspicion in this case of collusion to confer jurisdiction on the federal courts. Petitioner has, indeed, expressly admitted in his answer "that this suit is not a collusive one to confer on a court of the United States jurisdiction of a case of which it would not otherwise have cognizance" (47). The other purpose underlying the doctrine invoked, that stockholders must attempt to induce the directors to act before resorting to equity, was to prevent undue interference with the management of corporations by their duly elected officers. Such interference, however, is a matter of which only the directors can complain. The doctrine is not designed to protect wrongdoers. Here the Bank is not petitioning for issuance of certiorari; only Herbert Fleishhacker, seeking to avoid restitution of the profits of his wrongful acts. We respectfully submit that the objection that the court has unduly interfered with the management of the Bank by its directors is not one which the petitioner is entitled to assert.

The particular respect in which petitioner claims the evidence is insufficient is in the showing that the directors' refusal to sue was wrongful. As stated by Mr. Justice Hughes, expressing the majority opinion in *Ashwander v. Tennessee Valley Authority*, 297 U. S. 297, 319, 80 L. Ed. 688, 696:

> "In such a case it is not necessary for stockholders—when their corporation refused to take suit-

> able measures for its protection—to show that the managing board or trustees have acted with fraudulent intent or under legal duress."

It was enough in the instant case that the directors violated their duty to the Bank and its stockholders by failing to make a reasonable investigation of the respondents' charges, but instead endeavoring to confirm to petitioner the fruits of his fraud. The discretion of directors to refrain from seeking redress of wrongs done to the corporation is not unlimited. They must use diligence to determine the facts and must exercise reasonable judgment. As stated in *Kessler & Co. v. Ensley Co.* (C. C., Ala.) 129 Fed. 397, 408-9:

> "When all disinterested and fair men, upon the facts upon which the directors' act is challenged, would reach the conclusion that the decision not to sue was improper, and greatly prejudicial to corporate interests, and it appears that the directors have been negligent, or have not deliberated or passed judgment on the merits of the question, and refused to sue for some extraneous reason, or upon a mistaken view of the law, the court cannot refuse to intervene, although the directors may have been honest and disinterested."
>
> . . . . . .
>
> "They have the undoubted power to pass upon the question of redressing frauds upon the corporation, but it is a qualified authority in the employment of which they must use diligence to learn the facts, and exercise reasonable judgment upon the merits of the matter. If they act upon such matters negligently, without considering the good of the corporation, and are moved by extraneous considerations to wrong and injurious results, they commit a breach of trust.

> The directors under no circumstances have the right to gratituously and capriciously abandon or give away the rights of the corporation, either to a stockholder or to a stranger. Whenever it clearly appears that they have done so, a clear breach of trust is shown, and the courts will disregard such action."

In this case, before bringing this action, the respondents, through their authorized representative, Etienne Lang, made a written demand upon the Board of Directors in which they set forth what are admitted to be serious charges against the petitioner (30, 71-72). In acknowledging receipt of this demand the chairman of the Board stated that he would communicate with Lang later (588). No such communication was ever sent or received (587). No request was made that Lang appear and offer proof of the charges made. The Board merely passed a resolution that the claim had "no legal or moral basis" and that no action be taken (72-73). The only possible conclusion to be drawn from these facts is that the directors failed to exercise reasonable diligence or judgment in protecting the interests of the Bank and merely accepted petitioner's denial of wrongdoing.

The very nature of the charges against petitioner made it the duty of the directors to seek redress. By a criminal act (Petn. 2) petitioner had received and retained large sums of money which in equity belonged to the Bank. In a similar suit, to recover secret profits made by a promoter, *Groel v. United Electric Co. of New Jersey*, 70 N. J. Eq. 616, 61 Atl. 1061, the court said:

> "It is perfectly clear that, if the complainant sets forth a good cause of action and there is a right in

> the corporation to recover $20,000,000 of stock from the promoter, it is a clear breach of trust on the part of the directors not to proceed to recover the same. For them to reply that it is by them deemed inexpedient to do so is only to emphasize the breach of trust they are committing by not doing so."

The soundness of this principle was conceded by petitioner in the court below, and he in effect waived the point now urged as a ground for certiorari. As stated in the opinion of the Circuit Court of Appeals (911), quoting from petitioner's brief, he "freely admitted" that the taking of a bonus "cannot be ratified by the Board of Directors . . . so as to prevent suit by the bank *or a stockholder in its behalf* for its recovery."

Furthermore, as pointed out in the opinion of the trial court (196), the directors thereafter "made common cause with Herbert Fleishhacker in seeking to justify his acts." They joined the Bank with Fleishhacker in an answer asserting the perfect propriety of his transactions with the Bardes. Under such circumstances, even the formality of a demand is excused.

Kleinschmidt v. American Mining Co., 49 Mont. 7, 139 Pac. 785, 788;

Wickersham v. Crittenden, 106 Cal. 327, 331, 39 Pac. 603;

Dundon v. McDonald, 146 Cal. 585, 589, 80 Pac. 1034, 1036.

The exclusion of evidence referred to by petitioner (Br. 40-43) cannot be reviewed for want of a proper offer of proof in the trial court. The ruling complained of was the refusal to permit Mortimer Fleishhacker, petitioner's witness, to answer the question whether, *in relation to certain other litigation* instituted against the Bank in 1933, he had investigated the facts (631). The purpose, counsel stated, was to show why the witness, the chairman of the Board of Directors of the Bank, "refused to take seriously" the demand made upon the directors by Etienne Lang as agent for the respondents. Counsel, however, did not state what the testimony of the witness would be, and the offer of proof was therefore insufficient.

4 *C. J. S.* 580;

Price v. United States (C. C. A. 5), 68 Fed. (2d) 133, 135;

Kline v. Blackwell (C. C. A. 5), 63 Fed. (2d) 897, 899;

Schnerb v. Caterpillar Tractor Co. (C. C. A. 2), 43 Fed. (2d) 920, 923;

Chevrolet Motor Co. v. Gladding (C. C. A. 4), 42 Fed. (2d) 440, 445;

Sacramento Suburban Fruit Lands Co. v. Miller, (C. C. A. 9), 36 Fed. (2d) 922;

Ladd v. Missouri Coal & Mining Co. (C. C. A. 8), 66 Fed. 880, 882.

In the Assignment of Errors, filed after the decree had been entered, counsel for petitioner, for the first time, inserted a statement of the evidence sought to be adduced (792-4); but this offer of proof came too late.

Merz v. Poole, 82 Cal. App. 12, 15, 254 Pac. 914, 915;

Dougherty v. Ellingson, 97 Cal. App. 87, 98-9, 275 Pac. 456, 461.

The fact that respondents owned but a few shares of stock (Br. 43-44) has recently been held by this Court to be immaterial.

Ashwander v. Tennessee Valley Authority, supra, 297 U. S. 297, 318, 80 L. Ed. 686, 695-6.

III.

Certiorari Should Not Be Granted Because of Alleged Insufficiency of the Evidence to Negative Laches.

The second reason assigned by petitioner for issuance of certiorari is stated as follows (Petn. 24):

> "The court below has decided an important question of law in a way conflicting with applicable local decisions, as well as decisions of this Court, and has applied the rule of laches and the statute of limitations in such a way as to open the federal courts to unlimited speculation in stale charges of fraud."

An examination of petitioner's argument on this point (Br. 44-67) discloses the fact that the so-called "important question of law" is merely another question as to the sufficiency of the evidence. The Circuit Court of Appeals, in its opinion (911-912), fully recognized the necessity for proof that the Bank, as distinguished from the respond-

ents, failed to discover petitioner's breach of trust until within three years prior to the commencement of the action; but the court held the proof of this ultimate fact was sufficient, and it is this determination which petitioner now insists is an erroneous decision of "an important question of law". Here, again, we protest that petitioner is asking the Court, contrary to its established practice, to grant certiorari merely to review the evidence.

In the trial court, the petitioner in effect conceded that the suit was not barred by laches. At the conclusion of the trial, as appears from the record (706), counsel for petitioner stated to the court:

> ". . . if Your Honor feels that Fleishhacker solicited or accepted in any degree whatever as a consideration for lending the funds of that bank anything of value the judgment must be for the plaintiff."

Inasmuch as federal courts of equity ordinarily follow state statutes of limitation by way of analogy, the ultimate question is whether the suit would be barred in the California courts by Section 338, subdivision 4, of the Code of Civil Procedure of that state. It is not true, however, that the state statute has run five times over (Petn. 52), or at all, for it is expressly provided in the statute that *the cause of action shall not be deemed to have accrued until discovery of the facts.* As stated in *Kelly v. Boettcher* (C. C. A. 8), 75 F. 55, 62, where the Colorado statute under consideration was to the same effect:

> "The practical result is that a suit in equity for relief on the ground of fraud would not be barred by laches in the state of Colorado in less than three years after the discovery of fraud, unless unusual circumstances made it inequitable to allow its prosecution."

The question here presented, of course, is not as to sufficiency of the pleadings, but of the proof.

Victor Oil Co. v. Drum, 184 Cal. 226, 242, 193 Pac. 243, 250;

Consolidated R. & P. Co. v. Scarborough, 216 Cal. 698, 705, 16 Pac. (2d) 268, 270-271.

There is some doubt in the present case at to whether an issue was properly drawn concerning the Bank's knowledge of the fraud. As stated in the opinion of the Circuit Court of Appeals (912):

> "The pleadings did not specifically frame an issue in respect of the Bank's notice or knowledge of the fraud. We doubt, therefore, that appellants are in a position to urge the bar of the statute in so far as it relates to the Bank itself."

However, since the court passed upon the question, we shall discuss the evidence which sustains the conclusion reached.

It must be remembered that very little evidence will suffice to establish a negative, in this case the absence of knowledge. A negative fact is never susceptible of exact demonstration, and for that reason proof is sufficient which merely shows its probability.

22 Corpus Juris 80-81;

Leonard v. St. Joseph Lead Co. (C. C. A. 8), 75 F. (2d) 390, 397;

Hamilton v. Pac. Elec. R. Co., 12 Cal. (2d) 598, 603-5, 86 Pac. (2d) 829, 831-2;

Schlake v. McConnell, 83 Cal. App. 725, 731, 257 Pac. 175, 178.

Furthermore, as was said in *Victor Oil Co. v. Drum, supra,* 184 Cal. 226, at page 241:

> "The courts will not lightly seize upon some small circumstances to deny relief to a party plainly shown to have been actually defrauded against those who defrauded him on the ground, forsooth, that he did not discover the fact that he had been cheated as soon as he might have done. It is only where the party defrauded should plainly have discovered the fraud except for his own inexcusable inattention that he will be charged with a discovery in advance of actual knowledge on his part."

During the trial of the case petitioner made every effort to show the extent to which his business association with the Bardes was known in the Bank. An examination of this evidence, however, shows conclusively that petitioner never disclosed to his fellow officers or even suggested to them the fact that he had agreed with the Bardes to raise the necessary funds, the greater part of which were subsequently loaned by the Bank. Neither was the Bank informed that petitioner's partnership interest was to be given him in consideration for causing the loans to be made. On the contrary, the officers of the Bank believed that petitioner was securing his interest by personally investing a large sum of money in the venture.

It must be remembered that the Bardes dealt only with the petitioner (367). Petitioner testified he discussed the matter with the members of the Bank's finance committee —Mortimer Fleishhacker, J. J. Mack, and Sigmund Stern (700), and that

> "I explained to them that this loan was going to be made in connection with a steel deal in which I was going to become a partner."

The rest of this conversation, however, is disclosed by the testimony of Mortimer Fleishhacker (624):

> "I knew that Herbert Fleishhacker was going into a venture with the Bardes and in connection with steel; and *I knew that Herbert Fleishhacker was to personally put up a large sum of money* and the Bardes were to match that sum."
>
> "In other words, a new company was to be formed in which Herbert Fleishhacker and the Bardes were to be partners, *and each in a substantial amount.*"

During the entire period between the making of the loans and the filing of the present suit, petitioner continued to serve as president of the Bank (654). The Bank's records, of course, merely disclosed that loans had been made to M. Barde & Sons, Inc., and that these loans had in due course been fully repaid. The other directors and officers, obviously, were not required to suspect petitioner of wrongdoing or to question his representations, for he occupied a position of highest trust. Unless something of an extremely suspicious nature came to their attention prior to receipt of respondents' demand, the Bank cannot be charged with acquiescence.

The failure of the Bank, during the years which followed the approval of the loans, either to take action against petitioner or expressly to absolve him from liability, in itself constitutes evidence of lack of knowledge of the facts indicating petitioner's guilt.

Anglo California Nat. Bank of S. F. v. Lazard (C. C. A. 9), 106 F. (2d) 693, 704;

Estate of Bridges, 263 Ill. App. 499, 508, aff'd., *Crimp v. First Union T. & S. Bank,* 352 Ill. 93, 185 N. E. 179;

Barney v. Quaker Oats Co., 85 Vt. 372, 82 Atl. 113, 119-120.

Had any such information come to the attention of an officer of the Bank, it must be presumed that he would in the performance of his duty, have communicated it to the directors.

Cincinnati, N. O. & T. P. R. Co. v. Rankin, 241 U. S. 319, 327, 60 L. Ed. 1022, 1026;

Jones, Commentatires on Evidence, 2nd Ed., Vol. 1, p. 358.

In that event the Bank, in the ordinary course of affairs, would have taken some action; for, as stated in Section 1963, subdivision 4, of the California Code of Civil Procedure, it is presumed "that a person takes ordinary care of his own concerns." It is further provided in Section 17 of the said Code of Civil Procedure that "the word 'person' includes a corporation as well as a natural person."

Lack of knowledge on the part of the officers of the Bank, once established as having existed in 1919, must be presumed to have continued until the respondents brought the facts to light. As stated in *Smith v. Capital Gas Co.,* 132 Cal. 209, 212, 64 Pac. 258, 54 L. R. A. 769:

> "A 'state of mind once proved to exist is presumed to remain such until the contrary appears.' (1 Greenleaf on Evidence, sec. 42.)"

To the same effect:

Ward v. Waterman, 85 Cal. 488, 502, 24 Pac. 930;

United States v. Darmer (D. C. Wash.), 249 F. 989, 990.

Here it must be remembered that the petitioner, who as president of the Bank for the entire intervening period, had it in his power to prove knowledge on the part of the Bank, failed to produce any evidence in rebuttal of the presumptions referred to. A finding in accordance with these presumptions was therefore justified.

IV.

Certiorari Should Not Be Granted Because the Trial Court Accepted Findings Prepared by Counsel for Respondents or Because of Asserted Discrepancies Between the Opinions of the Trial and Appellate Courts.

The third reason assigned by petitioner for allowance of the writ is stated as follows (Petn. 27):

> "The court below has departed from the accepted and usual course of judicial proceedings and has sanctioned such a departure by the trial court."

On December 4, 1937, the trial court directed counsel for respondents to submit findings of fact and conclusions of law, as provided in Rule 42 of that court (197). On March 5, 1938, counsel for respondents lodged their proposed findings and conclusions, after serving the same on counsel for petitioner (765). On March 26, 1938, counsel for petitioner filed a request for special findings and conclusions (244-263) and amendments, additions and objections to those proposed by respondents (264-287), but these were denied and overruled by the court on March 29, 1938. On this latter date the court signed without change the findings and conclusions proposed by respondents.

The procedure adopted, far from being a departure from the accepted and usual course of proceeding, was in strict conformity thereto. Rule 42 of the trial court (quoted in *Century Indemnity Co. v. Nelson*, 303 U. S. 213, 215, 82 L. ed. 755, 757) provided:

> "Within five days after written notice of the decision, the prevailing party shall prepare a draft of

the findings and, in an equity suit, of the conclusions of law, and deliver the same to the Clerk for the Judge and serve a copy thereof upon the adverse party, who may, within five days thereafter, deliver to the Clerk and serve upon the adverse party such proposed amendments or additions as he may desire.

If the prevailing party fails to present such draft as above provided, the adverse party may prepare a draft thereof and deliver the same to the Clerk for the Judge and serve a copy thereof on the prevailing party within five days thereafter.

The findings of fact and, where required, the conclusions of law, shall thereafter be settled by the Judge, and when so settled shall be engrossed within five days thereafter, and shall be then signed and filed."

Whatever criticism may be made of the practice of permitting counsel to prepare and submit drafts of proposed findings of fact, petitioner cannot claim prejudice where, as in this case, he was accorded an equal opportunity to present objections and propose amendments and additions thereto. It must be presumed that the judge exercised judicial discretion in considering what findings to adopt, and the mere fact that he adopted all those proposed by counsel for respondents does not show a failure to exercise such discretion.

Considering the parallel columns of excerpts from the trial court's opinion and findings (Br. 73-78), it should

be noted that the first comparison relates to paragraph V of the findings (296), but that the same objection was made in the trial court (269-270). The next finding referred to, that petitioner caused the Bank to make the loans, was eliminated in the substitute paragraph proposed by petitioner, and for the same reason now suggested (273, 277-8). In like manner, it will be found, petitioner brought all the other objections now made to the attention of the trial court. The fact that all were rejected makes it clear that the findings as signed constitute the final expression of the court's views on the evidence.

The minor variances between the interpretation given the evidence by the trial and appellate courts (Br. 88-90) do not evidence a departure from established procedure. On the contrary, as counsel for petitioner argued in the Circuit Court of Appeals, in a suit in equity the appellate court is not bound by the findings of the trial court and must determine for itself the weight and effect of the evidence.

Keller v. Potomac Elec. Co., 261 U. S. 428, 444; 67 L. ed. 731, 736;

McIntosh v. Leisk (C. C. A. 5), 95 F. (2d) 164, 166;

Kapiolani Maternity & G. Hospital v. Wodehouse (C. C. A. 9), 70 F. (2d) 793, 801;

Updegraff v. United Fuel Gas Co. (C. C. A. 6), 67 F. (2d) 431, 432.

Conclusion.

The petition and supporting brief clearly show that the only reasons suggested for issuing certiorari in this case are that the trial court, after full consideration of petitioner's objections, signed the findings proposed by respondents without change, and that the evidence is alleged to be insufficient to support the judgment as to petitioner's breach of trust, respondents' right to maintain the suit, and the absence of laches. Petitioner in effect ask this Court to grant him a third hearing on the evidence. We respectfully submit that certiorari should not be issued for that purpose and, in any event, that the evidence fully supports the judgment.

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